Microfinance Dilemma

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Wetenschapswinkel
voor Economie

Microfinance Dilemma:
The Case of Bandung, Indonesia

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EC 124

2002

Microfinance Dilemma,

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Groningen, July 2002

Groningen University Economic Science Shop
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CIP-GEGEVENS KONINKLIJKE BIBLIOTHEEK, DEN HAAG

Microfinance Dilemma -The Case of Bandung, Indonesia, A. W. Brouwer, D. Dijkema, Groningen: Groningen University Economic Science Shop (Publications of Groningen University Economic Science Shop, EC 124)

- With references.

ISBN 90-5803-021-0

NUGI 682

Druk: Universiteitsdrukkerij Rijksuniversiteit Groningen

Preface

This paper contributes to the literature on microfinance by examining a relatively new microfinance programme that was started in 1996 at the Parahyangan Catholic University Centre for Community Services. Most of the data for this research was collected during a three-month stay in Bandung, Indonesia. This stay was made possible by the Parahyangan Catholic University and the University of Groningen, Department of Economics.

Before we come to the hard substance our research, the writers want to thank several people for their contribution to this paper. We thank our counsellors Dr. C.L.M Hermes, Dr. B.W. Lensink and Dr. L.J.R. Scholtens. This paper could not have been written without the hospitality of the Community Centre. We would like to thank Mr. Suroso and the other employees of LPKM for their kindness and their sincerity. Finally, we owe gratitude to Manto who always made time for us. For the patience and the conversations, even after the normal working hours and even when there were misunderstandings due to the language. Without his support, it would have been impossible to find the necessary data for our research. Thank you all for making this a learning process in more than one way.

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Groningen, March 2002

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Chapter 1 Introduction

There is not a more visible characteristic of economic underdevelopment than poverty. It is also the most shocking characteristic. Poverty not only threatens the existence of many people. By taking away the rights of a human being to live in good health, to obtain an education and to enjoy adequate nutrition, poverty destroys the aspirations, hopes of the future and enjoyment as well. Although the world has generated significant economic growth in per capita income, its track record on poverty is depressing. Over the period 1975-1985 consumption per capita in developing countries grew by 32 per cent, and rather by another 26 per cent over the period 1985-1995. However, by fairly conservatives estimates the number of poor people in the world is at this time approximately one billion (World Development Report, 1999). Most people would agree that the reduction of poverty should be a fundamental goal of society.

Despite these disappointing developments as far as the data on poverty is concerned, there are some promising new developments in the developing world. One of these is the focus of this study. Much excitement is based on a set of unusual financial institutions prospering in distant corners of the world especially in Bolivia, Bangladesh and Indonesia. Expectations were that much poverty could be alleviated by providing financial services to low-income households. And it has been proven that these expectations were not fantasies. These institutions, i.e. microfinance institutions, share the commitment to serve clients who were excluded by the formal banking sector and lack access to capital markets. Some of the programmes have primarily social missions, focusing on the outreach to women and measuring success in terms of poverty alleviation. Others aim to promote private sector activity in the face of unemployment and underemployment. As the transition economies are being restructured, microfinance has been put forward as a flexible tool to help individuals exploit new opportunities.

The Grameen Bank of Bangladesh has been in the vanguard of the ‘microfinance movement’, showing the potential to alleviate poverty by providing credit to poor households. The Grameen model emphasises market-based institutions that provide credit to poor households to generate new opportunities through self-employment. Grameen has reported repayment rates of 98 per cent and modest profits, while serving over two million functionally landless borrowers (Morduch, 1999). In accordance with the Grameen model, microfinance institutions have been established in many countries, for example in Bolivia, Chile, China, Ethiopia, Honduras, India, Indonesia, Malaysia, Mali, the Philippines, Sri Lanka, Tanzania, Thailand, the U.S., and Vietnam. In Indonesia the Bank Rakyat Indonesia (BRI) unit system is recognised as one of the largest and most successful microfinance institutions in the world.

Despite their appeal, the ability to help the poor rests on a set of propositions that must be proven rather than assumed in each empirical context. A lot has been written on the mechanisms that allow these programmes to successfully serve segments of the credit market, that commercial banks do not want to touch. These features include direct monitoring, regular repayment schedules, use of nonrefinancing threats, social capital, joint liability, group lending, et cetera. These mechanisms allow the programmes to generate high repayment rates from low-income borrowers. However, once the mechanisms worked reasonable well, standardisation and replication became top priority, with continued innovation receiving only marginal attention. However, simply replication is not appropriate, one must imitate and adjust to the circumstances.

One of the questions that naturally arises is whether the theoretical concepts apply and whether the mechanisms function as they are advertised. Most of the theoretical propositions are supported by anecdotes from particular programmes, but they have not been established as empirical regularities. Better research is needed to sharpen both the growing body of microfinance theory and ongoing policy dialogues. Empirical understanding of microfinance will also be aided by studies that quantify the roles of the various mechanisms in driving performance. One of the difficulties in these inquiries is that most programmes use the same lending model in all branches. Thus, there is no variation of which to estimate the efficiency of particular mechanisms.

There are several reasons to be interested in qualifying the roles of these overlapping mechanisms. This can benefit existing microfinance institutions in their design of savings and lending products, but it can also give new directions for further research. Gaining a better understanding of how programmes work in practice is necessary for developing innovations that can help to achieve the full promise of microfinance in developing economies. Therefore, the purpose of this research is to give an elaborate description and analysis of a relatively new microfinance programme. This is done by linking adverse selection, moral hazard, auditing and enforcement problems, caused by asymmetric information, to the practice of microfinance. Further, we link the literature on outreach and financial issues related to sustainability to this programme. However, it is not to say that these are the only subjects that need research and that play an important role in microfinance.

In an attempt to gain a better understanding and to shed light on the practical problems microfinance institutions face, we collected information on a programme that started in 1996 by the Parahyangan Catholic University of Bandung, Indonesia (UNPAR). At the University the Community Service Department Lembaga Pengabdian Kepada Masyarakat (LPKM) has been implementing comprehensive community development programmes. As the core activity in implementing the community development programme, the department facilitates the development of microfinance institutions. This department has been the centre of our research.

The data used for this case study at LPKM were collected in the period March until July 2001 in Bandung, Indonesia. The data were collected by interviewing the staff of LPKM, interviewing staff and members of the affiliated microfinance institutions in and around Bandung, attending meetings, and distributing questionnaires (see Appendix A and B) to the staff and the members of the microfinance institutions.

Data were collected by interviewing the staff of LPKM and is used to describe their microfinance programme. Our visits to some of the affiliated microfinance institutions and interviewing staff and members of these institutions provided a clear insight in the activities of these institutions. At meetings between LPKM and staff members of the microfinance institutions, there were again possibilities to interview and discuss with them. We used a questionnaire which is self administrated and standardised. The aim of the questionnaire was to describe and explain social phenomenon's especially to retrieve data on the specific social variables, group lending methodology, repayment, screening, meetings, the time cost of participation, and the services provided by the microfinance institutions to the members. Many of the questions were semi open-ended to retrieve useful information and we tried to formulate the questions as easy and understandably as possible.

The respondents of the questionnaires were staff members of the microfinance institutions and randomly selected members. The actual respondents were not disclosed to maintain anonymity, which was necessary to obtain accurate but sometimes sensitive information. The average number of staff members at the microfinance institutions is 5 and the number of members ranges from 20 members to over 400 members. We decided to distribute ten questionnaires to every microfinance institution, five for staff members and five for the members. At the moment of distributing the questionnaire, there were 21 microfinance institutions affiliated to LPKM. From the 21 institutions 3 had no activities at that moment and where therefore excluded from our research. In total we received 65 questionnaires from staff members and 63 questionnaires from members. The non-response was around 28 per cent. Due to various reasons not all distributed questionnaires were received back. For instance not all affiliated microfinance institutions were active at the moment of distribution, internal problems at microfinance institutions, the tight time schedule, et cetera made it impossible to receive back all questionnaires. The results of the questionnaires together with the data collected by the interviews was used in our research.

By looking at the relatively new programme at LPKM UNPAR from another point of view, we hope that the results of this study can help the University to provide services on an equitable, sustainable and widespread basis. We would also like to accomplish a diminishing of the gap between theory and practice.

The paper can be divided in three parts. Part one is the theoretical framework for the paper. It starts with defining and explaining adverse selection, moral hazard, auditing and enforcement problems, which will enhance the understanding of the negative effects caused by asymmetric information. This part also reviews the solutions used by microfinance institutions to deal with asymmetric information. Furthermore, the mechanisms and literature on outreach and financial issues related to financial sustainability is reviewed. The second part is descriptive. Chapter 3 gives an introduction to the Community Centre at the Parahyangan Catholic University. In chapter 4 the affiliated microfinance institutions are discussed. Attention is given to the affiliation of new institutions and the staff of the institutions. The third part gives an analysis of the programme by making use of the theoretical basis provided in part one of this paper: chapter 5 analysis the activities that are performed to withdraw and spread information to alleviate the problems caused by asymmetric information. The outreach of the microfinance institutions is outlined in chapter 6. The main question to be addressed is what the institutions do to reach their clients. It becomes clear that LPKM is more than a financial service provider. A better way to address the activities is by looking at LPKM as a social service organisation. In chapter 7 we look at LPKM and the institutions from a financial perspective. Finally, chapter 8 contains the conclusion of the thorough description of the programme.

Chapter 2 Theoretical concepts

In this chapter we will pay attention to theory and empirical findings related to the topics that will also be addressed in the case study. The theoretical concepts we describe are the problems resulting from asymmetric information, outreach of the microfinance institutions, and financial issues that are often discussed in the modern microfinance literature. In the case study these concepts will be discussed again and related to the practice. The common solutions to asymmetric information will be discussed in section 2.2. With our empirical research we also want to illustrate practical problems that can arise when providing services to the poor that an ordinary commercial lender would not want as customers. We do not address all theoretical concepts mentioned in the literature; however this does not mean that such mechanisms are not important on the contrary.

For many people it is hard to find a job, especially in times of economic crisis when the unemployment rate rises. For these people a solution to survive is to set up their own small-scale enterprise. This is not easy for them because they lack capital and collateral, and therefore it is almost impossible to obtain formal bank loans. An alternative solution is to join local co-operatives or microfinance institutions, where they may obtain small loans at low interest rates. These loans are based on trust and good business proposals, but due to a lack of financial security they are rather risky investments. Hence, the lack of collateral enhances the need to obtain relevant information. To decrease the risk microfinance institutions are searching for collateral substitutes and innovative alternatives to obtain information on the borrower.

Microfinance programmes around the world show many different approaches in providing financial services to the low-income households. They are all inspired by the common thought that lending to the poor can be financial sustainable. These programmes were set up by trial and error. The institutions learned from each other and from their own experiences. However this often lead to pure imitation, without any attention being paid to the specific political, social and economic environment. As a result most programmes are not optimally designed and do not necessarily offer the most desirable financial products.

§ 2.1 Asymmetric information

Asymmetric information refers to the uneven distribution of information among different economic entities. The withholding and twisting of information results in problems, which is characteristic of the relation between the principal and the agent. The principal and the agent act individually, in their own interest and with a certain degree of opportunism, in a world of asymmetric information (Bouma and Van Helden, 1994). Two types of informational problems are known to have significant effects. One is the problem of hidden information; the second is that of hidden action, often called the issue of moral hazard.

Terms like peer pressure, social capital, non-financial sanctions, are often used in the literature. One can easily loose track on how the various variables interact and the precise effect on the success or failure of these nonstandard loan contracts. We draw on the article of Ghatak and Guinnane (1999) to illustrate how microfinance institutions can overcome the problems of lending to the poor. Even though their focus is mainly on group lending and on how it can alleviate the problems of lending to the poor, it gives a comprehensive and systematic overview. By relating the problems with the group lending contracts the theoretical concepts and other mechanisms become clearer. Ghatak and Guinnane (1999) distinguish four major problems moneylenders are faced with due to asymmetric information. These problems are:

- adverse selection;
- moral hazard;
- auditing costs;
- enforcement.

It has become increasingly apparent that the incompleteness and asymmetry of information between agents have a strong influence on market structures, the nature of economic transactions and the kind of contractual arrangements people enter into.

One source of market failure is an imbalance of information between parties at an exchange, an imbalance that can be so severe that exchange is impeded. Asymmetric information can lead to adverse selection as well as to moral hazard. The consequence is that parties bear risk partly caused by chance and partly by the untrustworthiness of the contract partner who is taking advantage of his[1] “information lead”. The latter can arise in several forms. Firstly, a party can under false pretences persuade the other party to enter a contract. Reaching a transaction with somebody who you would rather not want to be your opponent and which is also determined by a form of deception, is known as adverse selection. Adverse selection arises in credit markets when customers have characteristics that are unobservable to the lender but that affects the probability of being able to repay the loan. A lender can solve this by assessing these characteristics or by offering loans that only good risks will accept. The typical method used by commercial banks, i.e. asking borrowers to pledge collateral, is not a realistic option, because the poor have limited supplies of tangible assets.
Secondly, it is possible that a contract, once closed, is not performed as it should be; e.g. the agent goes shirking, but tries to make out like the principal belief that unforeseen circumstances are the cause of the unsatisfactory result. One of the parties commits a hidden action, which means a type of behaviour that is not listed in the contract. Usually this results in actions taken by the agent in his own interest and not in his client’s. This form of risk is defined as moral hazard. It concerns the probability of disadvantages that are a result of absence of good faith, without incontestable proof for this (Bouma and Van Helden, 1994). The key element is that the actions are not costlessly publicly observable. In

the absence of collateral there is a conflict of objectives; the borrowers do not fully internalise the cost of project failure.

When a microfinance institutions gives a loan without security, it is even more important to audit the borrower. Therefore, the cost of lending for microfinance institutions are high. These institutions must take more measures to audit the borrower in order to secure repayment. Furthermore, it is sometimes very difficult for a moneylender to verify whether borrowers who say they cannot repay are indeed unable to do so. This is one of the many problems that result from asymmetric information.

The final problem distinguished by Ghatak and Guinnane (1999) is enforcement. In rural and urban credit markets there is substantial risk of default: the borrower might default on interest payments and even part or all of the principal. This risk has many causes. First, there is the risk of involuntary default: owing to sheer misfortune (crop failure, unemployment, disease, death, et cetera), the borrower simply may not have enough money when the loan matures. Second, there is the possibility of voluntary or strategic default: even if the borrower has enough resources to pay the loan back, the borrower may take the money and run, or simply refuse to pay. In regions where the legal machinery is not strong or functions slowly, this is not unlikely. The enforcement problem is related with strategic default and arises not from informational asymmetries but from the lender's limited ability to apply sanctions against a delinquent borrower. Weak legal systems, lack of securing collateral and the poverty of the borrower can substantially raise the enforcement costs.

§ 2.2 How to deal with asymmetric information

§ 2.2.1 Group lending

Group lending has taken most of the spotlight and with it joint liability in order to deal with problems caused by asymmetric information. Ghatak and Guinnane (1999) praise the innovation of group lending by referring to the apparent miracle of giving solvency to a community consisting almost entirely of insolvent individuals. Other theorists refer to the ability to deal with information and monitoring problems. Nevertheless, the role of group lending has been exaggerated. A paper by Aghion and Murdoch (1998) correctly points out that most studies have focused on the joint liability aspects and ignored other programme features. While it certainly has appealing features, there are other mechanisms that differentiate between microfinance contracts and standard loan contracts.

Group lending in general refers to making loans to individuals, while the group as a whole is held jointly liable should repayment difficulties arise. Many, and perhaps most, microfinance programmes are based on the concepts used by the Grameen Bank, especially when it concerns group lending.

[1] In this study the words 'he' and 'his' can be also read as 'her' and 'hers'.

According to the model, borrowers form groups of five persons. First, two members of the group get a loan. If they repay the loan on time, the next two get a loan, and finally the fifth gets a loan. This process continues as long as performance is satisfactory, but when a single member defaults all five members are excluded from future loans.

Many of these lending programmes ask borrowers to form a group in which all borrowers are jointly liable for each others loan, and most micro-lenders engage in intensive monitoring of clients and rely heavily on the promise of repeat loans for borrowers who perform well. The positive effect is that successful group members may have an incentive to repay the loans of group members whose projects have yielded insufficient return to make repayment worthwhile. Group lending with joint liability is just one mechanism driving the alleviation of poverty. Until now there is little empirical evidence on the relative importance of joint liability as opposed to the other mechanisms. Ideally, practitioners and academic writers would like to identify the precise factors that contribute to the failure or success of microfinance institutions, since there are more mechanisms at work. The overwhelming literature on microfinance, focusing merely on the incentives induced by joint liability in group lending contracts, suggests several reasons why unconventional lenders who lend to the very poor can do so with a reasonable degree of financial independence and astonishing repayment rates. But until now even theorists and practitioners are not sure what the genuine power behind the success of group lending is. Is it merely the formation of groups or the use of joint liability? Or should we simply focus on the other mechanisms?
To search for answers to these questions is worthwhile, particularly in light of the following evidence. Sadoulet (1997) argues that social collateral induced by group lending is not a sufficient condition to ensure high repayment rates, while Diagne (1997) points to the excessive cost of joint liability. Rai and Sjostrom (2000) have shown that the circumstances under which joint liability is optimal, are narrow and unlikely to hold in practice. Sharma and Zeller (1997) conclude that it is important for financial institutions to tailor services such that it becomes beneficial for the poor to establish a profitable long-term association; without this, the joint liability would quickly show poor results.

The use of joint liability can increase the performance of non-conventional lenders in some social context for two reasons. Firstly, members of a community may know more about each other than an outside institution does. Secondly, it is difficult for a financial institution to apply financial sanctions against poor people; as they do not have many possessions. However, the group is able to effectively use non-financial sanctions to discipline borrowers (loss of reputation, social isolation, restrictions on inputs, or physical force). The above mentioned reasons play a significant role in contracts with joint liability. However, gathering clients can also increase the performance of individual lending contracts by recognising that members can access complex and sensitive information, and by the imposition of sanctions (see the casestudy).

Group lending and arranging regular meetings mean adverse selection by drawing on local information networks. The main argument is that group members can obtain information regarding the reputation, creditworthiness, and wealth of the loan applicant and about his efforts to ensure repayment of the loan at a lower cost compared to socially and physically distant bank agents. This leads to a higher repayment rate and efficiency (Zeller, 1998). Group lending mitigates the problems of moral hazard by inducing members to influence the way other group members select their projects and their effort. Ghatak (1999) concludes that as long as social sanctions are effective enough or monitoring costs are low enough, joint liability lending will improve repayment rates through peer monitoring. Individual members bear liability for themselves but also for others in their group, i.e. internalisation of failure. As illustrated by Morduch (1999), this conclusion allows the bank to earn extra income from the joint liability payments, and the bank can afford to lower the interest rate. Thus, group lending increases the welfare and raises expected repayment rates. If the costs of auditing are too high, a contract with joint liability can also reduce these costs and improve efficiency. The expectation is that if group members face a lower cost of verifying each other's output, the microfinance institution can avoid the cost of performing its own audit every time a borrower claims he has low output by inducing his partner to undertake liability for him. Only when the whole group states its inability to repay, the microfinance institution will have to incur auditing costs (Ghatak and Guinnane, 1999).

Social capital can also be useful to lowering these costs. Social capital provides a fund of available information that permits a community to interact in a way that would not be possible in an anonymous society. In short, person A knows what person B is doing. This gives the group members the advantage that they can easily and against low costs asses the reason why borrower A declares default. Only when the whole group announces its inability to repay the loan, the bank has to incur auditing costs. Hence, audits take place less often under joint liability, and therefore the expected audit costs are lower and so is the interest rate. Social welfare is higher because joint liability makes lending to the poor possible, who are neglected by the commercial banks.

While group lending has many potential benefits, there are also disadvantages. One problem is that attending group meetings and monitoring one's fellow members can be very time consuming and therefore costly. A second problem is that the loan terms are limited by what the group feels that it can jointly guarantee, so members with growing businesses or new opportunities may find that the group contract prevents them from profiting from these opportunities. A possible explanation for this phenomenon is that the terms and conditions of the group no longer fulfil the demand of each group member in consecutive loan cycles, leading one or more members to default. Third, under some conditions group lending can lead to deliberate default by borrowers that could and would repay their loan if they were offered an individual loan contract (Besley and Coate, 1995). Because the group is shut off from future credit if other group members cannot repay their instalments or if the whole group cannot repay, it can be beneficial for a borrower not to repay. A fourth problem is that group lending can be costly to implement. Evidence for this can be found in the MicroBanking Bulletin (1998), which shows that microfinance programmes that target the poorest borrowers generate revenues sufficient to cover just 70 per cent of their full cost.

How well a group enforces repayment depends among other things on the degree of social and cultural cohesion but also on the quality of group leadership and size of the group. As Zeller (1998) notes, with increasing group size economies of scale, scope and risk management can be realised by the group. Also, the loan officer can visit larger groups more often, because unit cost per member tends to be lower. However, internal management problems, co-ordination and monitoring costs can outweigh the benefits of forming a group if group size becomes too large. Groups beyond a certain size may experience difficulty of communication and co-ordinating, so that both information and monitoring advantages of group formation are reduced and social cohesion may be less strong.

§ 2.2.2 Other solutions

Besides group lending contracts there are other instruments to enforce repayment. In some circumstances the only sanction a microfinance institution can impose on delinquent borrowers is not to refinance them (dynamic incentives). Again, social cohesion (as in friendship, family ties, social class, ethnic groups, and neighbourhoods) can provide incentives to members to respect the loan agreement with the microfinance institution. The meetings between the staff and the clients are an instrument to build and strengthen social capital and to exploit social cohesion among members. If a borrower now decides not to repay the loan, even if the financed project is a success, he incurs sanctions from the microfinance institution but also from his fellow group members. The members can rely on social sanctions that reduce the attractiveness of intentional default, and accordingly repayment rates will be higher. Dynamic incentives can be used to enforce repayment from borrowers. The effectiveness of this threat depends among other things on the availability of other moneylenders and the willingness of members to move or to find for them.

In areas with relatively low mobility dynamic incentives will work better. In urban areas, for example, where households come and go, it may not be easy to catch defaulters who move across town and start borrowing again with a clean slate at a different microfinance institution. Evidence for this can be found by looking at Bank Rakyat Indonesia, which has faced greater trouble securing payments in their urban programmes than in their rural ones, perhaps due to greater urban mobility. The spread of information can undo but also strengthen the effects of the mobility of clients of microfinance institutions. Lack of information can increase the probability of borrowers moving to other areas. In the informational sophisticated credit markets that prevail in industrialised countries, credit histories are easily tracked down on a computer; a bank or institution can easily learn about a person’s past, and the ability to obtain this information quickly acts as a device to discipline the borrower. Certainly, this is not a realistic postulate in credit markets in underdeveloped countries. The low mobility of borrowers can also help to explain advantages found in lending to women. At Grameen, for example, 15.3 per cent of male borrowers missed some payments before the final due date, while this was true for just 1.3 per cent of the women (Khander, Khalily and Kahn, 1995).

§ 2.3 Outreach

The main objective of the microfinance institutions is poverty reduction, so they often wish to focus on the poorest segments of the population. In the field of microfinance there is much debating on whether access to financial services benefits “the poorest of the poor”. A study by Hulme and Mosley (1996) on whether microfinance is appropriate for these poorest of the poor shows that clients below the poverty line were worse off after borrowing than before. Their findings suggest that successful institutions contributing to poverty reduction are particularly effective in improving the status of the

middle and upper segments of the poor. By aiming too much at the poorest of the poor (and female), selection bias may take a negative turn. Pitt and Khandker (1998) look at the impact of group based credit programmes on poor households in Bangladesh. They find that poorer households are more likely to be borrowers than their neighbours, depending on village of residence and other observable characteristics. In cross-sectional studies this outreach towards the poorer households can lead to a downward bias on the estimated effect of credit on earnings. In extreme cases, the effective targeting of poor households can yield the impression that participation in the programme makes clients poorer.
Besides serving the poor, the objective of many microfinance institutions is to empower women by improving their economic position in society. The public transcript of the Grameen Bank for targeting women is based on two objectives. First, to give women access to credit to increase their earning capabilities and bring improvements to the household socio-economic conditions faster. Second, to organise women into groups to raise their collective consciousness, strengthen their group solidarity though weekly meetings and assist them in attaining greater socio-economic power in society (Rahman, 1999). But the microfinance programmes did not begin with a focus on women. At Grameen in 1980-1983 women made up 39 per cent of their membership and at Bangladesh Rural Advancement Committee (BRAC) 34 per cent were women. But by 1991-1992 at BRAC membership was 74 per cent female, and at Grameen it was 94 per cent female (Goetz and Gupta, 1995). How did this number of female members increase so quickly? The first explanation can be found it the lower mobility of women, which decreases moral hazard. The risk that women will take the money and run is much smaller than for men (Murdoch, 1999). Dynamic incentives can also help to explain advantages found in lending to women. Because women have fewer alternative borrowing possibilities than men, dynamic incentives will be increased (see subsection 5.4).

The loans provided to women are not always used by the women. According to Rahman (1999), the loans are extended to women, but in his community study at the Grameen bank it shows that predominantly men use these loans and supply instalments to women for their weekly repayment in the loan centres. Goetz and Sen Gupta (1995) find that although 95 per cent of Grameen borrowers are female, in just 37 per cent of these cases do female borrowers retain significant control over use of the loan (Morduch, 1999).

Another aspect of outreach is whether the programme serves rural or urban clients. Institutions in an urban area have both advantages and disadvantages. The advantages of serving urban members may include (Morduch, 1999):

- lower transaction cost (shorter distance to microfinance institution);
- increased possibility that clients are literate;
- potential higher chance of repayment, since interactions with clients can be more frequent;
- possible leveraging through relationships with formal financial institutions, since urban clients may be physically closer to formal sector banks and more comfortable with visiting banks;
- more developed local infrastructure and more varied markets.

However, urban clients may be more transitory, which can result in a higher risk of potential default (moral hazard), character based lending may therefore be more difficult. In addition, there can be covariance risk if most clients are active in the same economic sector. In the urban area more alternative borrowing possibilities exist, which may decrease the use of incentives that spring from not refinancing delinquent borrowers.

But rural markets also have disadvantages:

- there may be a long history of poorly designed rural credit programmes (with subsidised credit, no savings mobilisation, or credit tied to specific activities or purchases);
- there may be a less diversified economic base;
- covariance risk can be significant: like with agricultural lending, many farmers may grow the same crop, resulting in a higher risk in case of drought or other climate disorder;
- there may be no branch or formal financial institutions in the area. This can create problems when clients need access to branch network for savings deposits or loan repayment;
- it may be more difficult to reach the minimal scale required to break even;
- there is likely to be a poorly developed infrastructure and a more dispersed population.

Also many government-sponsored programmes that offer rural credit have resulted in disappointing performance due to their reliance on subsidised interest rates, inappropriate terms and conditions, a lack of repayment enforcement and corruption (Morduch, 1999).

§ 2.4 Issues related to financial sustainability

§ 2.4.1 Costs of microfinance institutions

The practices that formal banks use to gain confidence in the quality of their loan portfolio are very expensive and can only be used when the size of the loan is large. They commit credit checks, pledging collateral and time-consuming appraisal of business plans. The high costs involved and the small size of the loan makes donor funds necessary. Another reason is that the microfinance institutions not only offer financial services but also non-financial services. These services are teaching the poor to manage their loans. These services will be addressed in subsection 3.3. The costs associated with these non-financial services are considered as social costs (sunk costs) that are needed to do business with the poor (social investment). These costs should be subsidised since no institution can offer financial services and at the same time cover these costs. This is the argumentation of advocates of subsidies. Yet, there are arguments used by people who tend to believe that subsidies are not needed and that it is possible for microfinance institutions to generate enough revenues to cover the cost.

For a microfinance institution to stand on its own feet, it has to be financially sustainable. If a microfinance institution wants to be financially self-sufficient, it must cover operating costs and finance costs through fees and interest charges. There are many roads a microfinance institution can follow to recover all costs, but charging a higher interest needs more attention and research. In Indonesia there is a difference between commercial interest rates and the rate charged by microfinance institutions. So the microfinance institutions can charge a relatively high interest rate, while they are still attractive to poor households. Rhyne and Otero (1992) also state reasons why this can be a benefit to the microfinance institutions. Moreover, it appears that clients of microfinance institutions are more sensitive to the availability and convenience of credit than to the interest rate (Christen, 1989). Research to the elasticity of credit demand is very valuable in this context. Nevertheless, there would be trade-offs. Borrowers will have more difficulties repaying, as a result default rates are likely to increase. And it can undermine the social goal of the programme.

§ 2.4.2 Savings services

Savings services are often not available to clients of microfinance institutions, for two main reasons. First, it was thought that the poor were too poor to save. Second, due to the regulatory constraints of most microfinance institutions, many of these are not legally allowed to mobilise deposits. However, recent microfinance evidence shows that even poor households want to save. Mobilising savings can have substantial benefits, if proper precautions are taken. In addition, there must be a suitable economic and political environment in the country in which a microfinance institution is active (World Development, 2000), because this environment influences the ability of a microfinance institution to offer savings services in a sustainable manner. For instance, Bank Rakyat Indonesia already offers four savings instruments carrying different interest rates and liquidity features. One of these is the SIMPEDES saving programme which is very successful, even if the interest rate is zero for small deposits, 0.75 per cent monthly for medium deposits and 1.25 per cent monthly for larger deposits (Charitonenko, Patten and Yaron, 1998). The BRI Unit Desa System in Indonesia is now fully financed by savings, so it is proven that collecting savings from poor clients is possible.

§ 2.4.3 The role of subsidies and repayment

Even large microfinance institutions such as Grameen Bank need continuous subsidies, and a recent survey shows that the microfinance programmes that target the poorest borrowers generate revenues sufficient to cover just 70 per cent of their full costs (MicroBanking Bulletin, 1998). A common criticism of subsidies is that it sometimes may fall in the wrong hands. Microfinance institutions that receive subsidised funding are less likely to effectively manage their financial performance since they have little or no incentive to become sustainable.

A question that arises is naturally whether these subsidies should continue, since a hands-off policy is desirable in any market only if all other markets are working properly. There are signals that the credit market in transition economies has market failures, and this provides a rationale to intervene in the form of subsidies. Even if the credit market is functioning perfectly, subsidies may be justifiable on grounds of equity. Simple calculation of the costs and benefits of subsidies is very difficult, and when it is attempted problems may arise. All benefits and costs should be taken into consideration, but not all benefits and costs can be measured easily and objective. First of all there are non-pecuniary benefits. For example, how does one measure increased power of poor individuals, increased education possibilities, the presence of savings opportunities, and shifts in attitudes. Certain merits are hard to quantify, and to make it even more complex there are externalities. Second, extending a loan to a member can create benefits for another individual, the so - called spillovers. Third, Hoff and Stiglitz (1998) illustrate cases in which the existence of a subsidised microfinance programme worsens the terms and availability of loans offered by moneylenders in the formal sector.

Microfinance discussions pay surprisingly little attention to these particular mechanisms as compared to how much attention is paid to purely financial matters. Attention mainly focuses on the determinants that influence repayment performance. Theoretical models have been developed to explain repayment performance of microfinance institutions, but so far empirical analysis to test them is extremely scant. To provide an insight into the financial status of the microfinance institution, repayment rates are often used. By calculating these rates, the efficiency and viability of the microfinance institution can be determined. These rates measure the amount of payments received with respect to the amount that is due. There are many ways to calculate the repayment rates of microfinance institutions, which makes it difficult to compare the repayment rates of different programmes. The reported repayment rates are often quite high, but many microfinance programmes are also subsidised. This leads us to the question whether the repayment rates are accurately measured and the role of subsidies in the calculation of the rates. Nevertheless, insight into repayment rates and the influence and amount of subsidies make the programmes more transparent.

Chapter 3 The Parahyangan Catholic University Centre for Community Services

In Indonesia since 1995 every University is required to have a Centre for Community Services. This rule is enforced by the Education Department and its purpose is to make universities socially active in their local area by doing: research, providing basic needs to the poor, providing help to build irrigation systems, et cetera. The Centre for Community Services (Lembaga Pengabdian Kepada Mayarakat, LPKM) at the Parahyangan Catholic University (UNPAR) has been the centre of our case study[2].

In subsection 3.1 we will give an introduction of LPKM. Next, the vision of LPKM will be described, followed by the activities of LPKM. In section 3.3 the non-financial services will be addressed. Finally, the working environment of LPKM is described by looking at other providers of financial services.

§ 3.1 Introduction LPKM

LPKM is the co-ordinator and assistant of the creation of microfinance institutions in West Java. The people at LPKM give supportive facilities to the microfinance institutions, which in turn provide cheap loans to develop small-scale enterprises. LPKM extends loans only to the microfinance institutions and does not interact directly with the members of the institutions. At this moment LPKM has assisted the development of 21 microfinance institutions, and the total number of members of the institutions is around 2000 (at the end of 1998 there were eight microfinance institutions affiliated and the number of members was 850). LPKM raises funds from individuals in the community, state-owned enterprises, non-government organisations, local government and from the university in the form of a revolving fund amounting in total to Rp. 183,000,000[3]. The total loan amount outstanding at the microfinance institutions is approximately Rp. 175,000,000 with the loan size varying from Rp. 1,200,000 to Rp. 61,200,000. From the data we obtained can be seen that loan sizes extended from the microfinance institutions to members can be as low as Rp. 100.000 and as high as Rp. 1,000,000; the average loan size is somewhere in the region of Rp. 835.000.

[2] Since the focus of the research is from the perspective of LPKM and based on our own experiences we make the following remark: the reader is reminded to keep in mind the descriptions and regulations that refer to the relation between LPKM and the microfinance institutions, and between the microfinance institutions and their clients.

[3] Exchange rate 1=Rp. 9,300 (May 2001).

LPKM charges a moderate interest rate to the institutions (4 per cent per year), which in turn charge a low interest rate to their members (2 per cent per month) and adhere to the basic principles that are recognisable in microfinance programmes elsewhere. The target is to assist and empower the poor in rural areas, as well as in urban areas. While the programme in practice tends to serve the richer clients of the poor, no collateral is pledged (see section 6.1). So if the members fail to repay, it is not possible to seize tangible assets such as livestock, land or housing to cover the cost or as a mechanism to enforce the agreements. LPKM and the affiliated microfinance institutions do not make use of eligibility criteria to exclude richer households.

While microfinance institutions all over the world have something in common, generally the programmes have a common thread that influences the organisation and institutional aspects of the specific programme. However each microfinance institution has a feature that makes it markedly different from its colleagues. When looking at the programme initiated by LPKM, there are six characteristics that make its design unique and distinguish it from other programmes.

First, the members who save at the microfinance institution do not receive interest. Instead, they can receive dividend at the end of the year with the obvious condition that the institution has yielded a profit. Second, interest rates on loans are fixed, independent of the intention of the loan or the characteristics of the borrowers. Third, the extent of co-operation between the institutions is very strong and will be strengthened in the future. Fourth, the design of the reward system to provide the appropriate incentives for the staff of the microfinance institutions. Also, the use of group lending contracts for large amounts is remarkable, since Armendariz de Aghion and Morduch (2000) show that there is evidence that this is not effective in achieving high repayment rates or in the best interest of the borrowers that already have growing businesses (non-starters). The final characteristic is the efforts and creativity of the staff of the microfinance institutions to create extra revenues. For example one institution is collecting garbage from people in the local area, the earnings after subtracting the cost will be retained at the institution and is available to borrowers. Another institution has been developed further; they recycle garbage and sell the output as fertiliser. An avenue that is also illustrative for the creativity and perseverance, is money collecting for phone bills: the staff gathers the money, transfers it to the phone company and receives a commission from the people in the area for this service.

Besides the core activity of providing finance and training to microfinance institutions, LPKM participates in an action programme to protect working children and to combat and eliminate child labour. To this end, they co-operate with the International Labour Organisation (ILO). LPKM first tries to retrieve data regarding small-scale footwear businesses in Cibaduyut (a district of Bandung), to understand the area and to identify reasons for the use of children in the production of shoes. By providing training (business ethics, financial management, human resource management) LPKM tries to assist in the development of the small-scale footwear industry in order to reduce the use of child labour. Other programmes started by LPKM are housing and kampung improvement, training programmes for organic farming, networking with non-government organisations (NGO’s) and health care. These side activities will be explained in more detail in the next subsections.

§ 3.2 Vision of LPKM

Preferential option for the poor in terms of individual, group or area, is the individual's or group's option to show solidarity and give priority to those who have not enjoyed the fruits of development, particularly those who are still living in poverty. Preference for the poor means that concern, special treatment and preference is given to people who are in need. The vision of LPKM is preferential option for the poor who are in need, as mentioned above, and to assist the poor to become self-empowered (Suroso, 2001).

§ 3.3 More than financial services

The microfinance institutions offer their clients a variety of services, but first and foremost they offer financial services. However, due to the nature of the target group of the microfinance institutions, i.e. poor households without tangible assets and with a majority that is illiterate, they cannot operate like most financial institutions. Ordinary financial intermediation is not enough to induce these low-income individuals to participate in the programme, and therefore microfinance institutions have to offer all kinds of (purely) non-financial services and create mechanisms to bridge the gap created by poverty, remoteness, illiteracy, malnutrition. These non-financial services range from vocational, social nutritional to entrepreneurial education. This is typical for the social goal that microfinance institutions want to achieve, and also there is evidence that social intermediation makes it easier to establish sustainable financial relationships with the poor.

From interviews with the employees at LPKM, we draw the conclusion that they view the provision of these social services as a process that is necessary to build the human and social capital required for providing effective financial services. Thus, LPKM hopes that the capacity, ability, attitude, skills and social capital of the staff (and members) of the microfinance institutions will develop. This will eventually contribute directly and indirectly to the performance of the institutions. By training and educating the staff of the institution the members of the microfinance institutions will also benefit. The microfinance institutions act as an intermediary because LPKM never provides training and education to the members directly.

Every month LPKM organises a meeting for the staff of the microfinance institutions. During the time of the research not all members were present (from the 21 institutions that were invited only 13 microfinance institutions showed up). The microfinance institutions are not forced to attend the meeting: no reprisals are being used when a microfinance institution does not come even when there absence was not announced. This meeting is also used to collect the instalments, and to hand in the financial reports and business proposals for new loans.

LPKM devotes a lot of resources to these meetings, they regard these meetings as an effective way to develop the microfinance institutions and increase the skills and confidence of new and existing microfinance institutions[4]. They are also aware that some of the microfinance institutions are not ready for sustainable financial intermediation without first receiving some capacity-building assistance.

LPKM is well-aware that loan contracts cannot function unless there is a clear statement by the underlying social contract and a clear and well-defined mechanism to punish deviations from the norm. LPKM tries to design the programme in such a way that social capital (and mechanisms) is build, developed and sustained. Earlier we stated several manners to start this process. Besides the non-financial services addressed in the former subsections, three other promising programmes (developing health care, kampung improvement, and collaboration with the ILO) must be mentioned, because it is illustrative of the character of these non-traditional financial institutions. These three programmes will also be developed within the framework of micro credit at LPKM.

§ 3.3.1 Health care

LPKM is collaborating with two Catholic hospitals, that have a programme for the grassroots people. The idea is to set up health clinics in the vicinity of existing microfinance institutions accessible only for the members. Until now there are two health clinics (Kebon Pisang and Kamuning near BMW Bandung and LPKM, respectively). At the moment, members pay Rp. 2,000 for a consult and the maximum co-payment is Rp. 18,000 for medication. LPKM, BMW Bandung and sponsors provide the financial resources that is needed to develop the clinics. It is proposed to arrange it like an insurance scheme (dana sehat bersama). Members have to contribute Rp. 2,000 per month for a family consists of a mother, father and two children to receive benefits from it. However, this insurance scheme has to cope with some issues since there is a problem concerning the (lack of) social capital. Several people pointed out that members are afraid that they do not get the money back once they have made a contribution to the fund. There has to be a gradual process of members gaining confidence and trust in the insurance. Despite its appealing virtues, providing health care services gives rise to specific problems: moral hazard, adverse selection, and transactions costs. To solve some of these problems a health committee will be created to determine if the people are really sick and need to go to the clinic or hospital.

[4] If the training requires the expertise that LPKM cannot (for instance agriculture), they search look for somebody who is capable of providing this training.

§ 3.3.2 ILO

LPKM also co-operates with the International Labour Organisation. The main objective is to remove child labour from a hazardous working environment in the footwear sector. LPKM and the ILO will strengthen the entrepreneurship and develop the management capacity of employers from the footwear sector to achieve this objective. Workshops are organised to change and transform culture and the way of thinking in almost all aspects. Employers will also participate in workshops on business ethics related to child labour.

§ 3.3.3 Kampung development

With respect to their mission in order to assist the poor to become self-empowered, LPKM has stretched its efforts to housing for the poor. The belief is that housing can stimulate repercussion effects in the community. First of all, it creates jobs and working opportunities for the community. It directly creates jobs in the field of construction and also in construction materials, such as wood, bricks, et cetera. Housing and neighbourhood improvement will also involve the securing of dwellers' land rights. Many people living in slums do not have proper legal documents to the land they own, which is also a major concern. Organising housing and kampung improvement projects will also improve co-operation among people in the community and help create a better atmosphere and culture. The microfinance institutions assist in providing loans to members who wish to improve their living conditions. This may involve repairing house, improving their sewage or waste system, or enabling people to obtain clean water, et cetera. People may also want to expand their house to accommodate the creation or expansion of home industry or other businesses that are run from the house, e.g. renting out rooms or opening up small kiosks where they sell basic goods, and providing services to customers in the community.

While LPKM addresses many issues related to the improvement of the well-being of individuals, the main focus of LPKM is providing micro-credit and building and developing microfinance institutions.

§ 3.4 Working environment

The role of LPKM in the total microfinance industry in Indonesia is still minor. The Bank Rakyat Indonesia (BRI) unit system is a very successful microfinance institution in Indonesia. It is owned entirely by the government, but operates under all of the prudential norms and regulations that every commercial bank must adhere to in Indonesia. BRI's primary mission is to provide rural and urban community banking services by mobilising family savings and delivering credit products to medium, small and micro enterprises. In 1997 BRI's total assets were $16.7 billion, including a net loan portfolio of $12.6 billion, and pre-tax profits totalled $56.7 million[5]. It had 324 branches that covered the entire country, overseas offices in Singapore, Hong Kong and New York, and a work office of 44,000 employees (Patten, Rosengard and Johnston Jr, 2001). Besides BRI there are other microfinance institutions, but they often operate on a smaller scale and in a certain area or district. On Java, for instance, there is a sister institution of BRI, Badan Kredit Desa (BKD); it is a system of village-based institutions. The units are owned by villages and operated by village governments. BKD units are located in the rural areas of Java. There are 5,345 units, of which 4,806 were active in 1996 (Ravicz, 1998).

The black market also provides credit to the poor households. It has its own methods to attract clients. The black-moneylender goes from door to door to ask people if they are interested in a loan agreement. The rate charged by these lenders is between 15 and 40 per cent per month (compare this with the 2 per cent of the microfinance institutions). If clients do not repay their loan on time, physical force will be used. Nevertheless, it can be very tempting for people who are in financial distress. Usually, the loan agreement is based on trust, and no collateral is required. In one area in Bandung, Dago Dago Elos Area, a microfinance institution (Kopmaba) competed with the black market and they made an agreement that black-moneylenders would not operate in this area anymore. Another microfinance institution (BMW Sumedang) claims that it has difficulties repaying their loans to LPKM, because the black moneylenders are very active in the area. The staff of BMW Sumedang asserts that their members first pay the black market participants, and only when they have no more debts at the black market they repay the microfinance institution. However, employees at LPKM cast doubt on this assertion. Also because another institution, which is situated nearby, has no trouble with the black market and its interference.
But if there are already so much microfinance institutions and other sources of credit, why has LPKM helped to create more microfinance institutions in Western Java? The microfinance institution is a vital factor that supports the entire economic activities in the community. Microfinance development is considered to be the entry point for total community development, which is the main purpose of LPKM. Besides, BRI and BKD only lend to the poor who are "better off" and the bank requires individual borrowers to put up collateral, so the very poorest are excluded (Morduch, 1999). BRI and BKD also provide loans that tend to be larger and they charge a higher interest, so therefore they are less focused on the poor.

Local people ought to manage the microfinance institutions, but they often lack skills for managing these institutions. In the first year, 1997, LPKM began assisting microfinance institutions, by only providing training. Training is not only given to develop skills, but especially to facilitate change and development in the business attitude and behaviour. Most of the affiliated microfinance institutions

[5] mid 1997 exchange rate of $1.00 = Rp. 2.450

only give loans and have saving facilities, but do not give training. LPKM's first loan to an institution was granted after one year. The loans are not based on commercial bank requirements, but on character and sound business proposals.

4. The microfinance institutions

Since the start in 1996, LPKM assists the creation of microfinance institutions in West Java, which provide loans for the development of small-scale enterprises. This is where LPKM has focused its efforts in order to alleviate the problems faced by the poor. They provide finance to microfinance institutions and co-operatives against a low interest rate. Furthermore, they provide training in organisational and accounting skills to the microfinance institutions.

An institution is a group of (human, financial and other) assets combined to perform activities such as granting loans and taking deposits overtime (Murdoch, 1999). In April 2001 there were 21 microfinance institutions (table 4.1) affiliated with LPKM. These institutions will be described in more detail in the next subsection when we look at the key characteristics. During the research period eight additional institutions applied to become affiliated with LPKM. The application procedure and the problems new institutions face when they first start with their activities will also be discussed in the following subsections. LPKM has strict criteria and information requirements for new institutions to combat moral hazard and adverse selection. On their turn the microfinance institutions in turn have rules concerning the acceptance of members to avoid the problems discussed in chapter 2.

§ 4.1 Strong microfinance institution

According to Morduch (1999) a good microfinance institution has three attributes. First, it must provide services to the relevant target group. Second, the activities and offered services must also not only be demanded but also have some identifiable positive impact on the lives of customers. Third, a good institution is strong, financially sound and stable. In a more comprehensive study by Fruman and Isern (1996), seven key characteristics of a strong microfinance institution are distinguished. The seven key areas, which are used to provide more insight into the strength of the affiliated institutions, are:

1. vision;
2. financial services and delivery methods;
3. organisational structure and human resources;
4. administration and finance;
5. management information system;
6. institutional viability; and
7. outreach and financial sustainability.

A mission statement is a characteristic of the first key area - vision. This statement must define the target market and services offered, and management and staff must endorse it. LPKM clearly has a well-defined vision (mentioned in chapter 3) which is adopted by the affiliated microfinance institutions. The reward system, which will be described in subsection 4.4, for staff members of an institution depends on the performance of the institution itself. This reward system makes the staff members very strongly committed to pursuing the institution to become a profitable niche (in terms of people and funds). Strong commitment by the staff provides a positive contribution to the strength of the microfinance institution. The third characteristic is a business plan, stating how to reach specific strategic objectives in three to five years. For the affiliated institutions it is very difficult to make such a business plan, because the activities are risky and much depends on the willingness of its members. However, LPKM makes a business plan with (for instance) objectives for the future together with or for the institutions.

The second key area, financial services and delivery methods, is characterised by the adoption of simple financial services to the local context and the clients. The institutions try to listen to their members in order to provide services they appreciate. By organising special meetings to its members, the staff is open to new ideas and suggestions to improve the institution. Another characteristic is decentralisation of client selection and financial service delivery. All affiliated institutions make their own decisions when they accept new members and grant loans to their members. Also for the provided services LPKM only gives advice. The chief or staff of the institution makes the final decision.

A characteristic of the third key area - organisational structures and human resources - is the use of accurate job descriptions and relevant training. Even though at every institution there is a clear distinction between the functions of the staff, they often have to do activities that are not in line with their job description. This is sometimes due to lack of number of staff members or lack of skills. The data from the staff members of the institutions shows that 36 per cent of the difficulties in the past had to do with staff members of the institution. For instance, bad co-operation between members of the staff and lack of skills, are two problems often observed. Loan enforcement seems to be a huge problem, especially when starting microfinance institutions, who face too many bad repayments and bad discipline from their members (23 per cent), according to staff members of the institutions. Secondly, the new institutions lack funds (13 per cent), and thirdly, their own administration is poor (12 per cent)[6]. To improve skills of the staff and alleviate the problems of new institutions, the staff receives training provided by LPKM. The training, such as book-keeping and entrepreneurship training, is focused on their work at the institution. In addition, a strong institution must have appropriate performance-based incentives offered to the staff. The reward system, as described in more detail in subsection 4.4, provides a very good incentive to the staff.

Fourthly, administration and finance is characterised by standardised activities and its understanding by the staff. Even though many administrative activities are standardised, almost all members need special treatment. Every member has its own loan agreement with a specific loan amount and specific

[6] An anecdote from one of the staff members tells that they there where problems with the opening hours of their institution. They came to LPKM to complain that it took a lot of time to run the institution. It turned out that they were open all the time and therefore there was never time to rest. LPKM advised the staff of the microfinance institution that it is better to have fixed opening times.

terms. Other administrative activities such as member and loan application are standardised. Also internal and external audits carried out at regular intervals contribute to the strength of the institution. Every microfinance institution is obligated to hand in a financial report monthly, which is audited by LPKM and employees and students of the Department of Economics.

The fifth key area is the management information system. This system is to provide timely and accurate information on key indicators that are most relevant to operations and are regularly used by staff and management in monitoring and guiding operations.

Microfinance information systems generally fall into three main areas (Morduch, 1999). First, an accounting system with the general ledger as its core. Second, a credit and savings monitoring system, which captures information and provides reports on the performance of each granted loan, often with a savings system that monitors all transactions related to member savings. The institutions affiliated with LPKM do not use an automatic credit and savings monitoring system, but they record all credits and savings and these data are monitored by staff and at some institutions also by the credit team. Also all the institutions have to hand in a financial report with the general ledgers, they also have to deliver a yearly report, Rapat Angota Tahunan (RAT), to LPKM. This report contains among others things information concerning outstanding loans, profit, and the total number of members. Third, information systems as distinguished by Morduch (1999) is a system designed to collect data on client impact. Even though the data from the staff shows that they collect data on the impact of the programme, generally the data is gathered only in an informal manner and not systematically recorded. Data gathered by the staff concerns increased income of the members and increased business skills, such as book-keeping or management (both 37 per cent). From the staff respondents, 21 per cent claims that they gather information about the investments in the business of the member, and 18 per cent gathers information on the children of the members: whether they receive more education and nutrition.
Legal registration and compliance with supervisory requirements is the main characteristic of the sixth area, i.e. institutional viability. All microfinance institutions want to have a legal registration to become a legal form. This legal form makes the institution appear trustworthy to potential members and it improves the viability. From the affiliated institutions thirteen institutions have a legal form, shown in table 4.1.

The last (and seventh) key area of a strong microfinance institution is outreach and financial sustainability. Financial performance will be dealt with in chapter 7. It is characterised by achievement of significant scale, including a large number of underserved clients (for example, the poor and the women). As can be seen in table 4.1, the number of members of the institutions ranges from 20 (minimum requirement) t0 426. Chapter 6 contains more information on the members served by the microfinance institutions.

Table 4.1: Microfinance Institutions

Institution		**Date established**	**Setting**	**Number of members**	**Legal form**
1.	BMW Bandung	March 1997	Urban	225	Yes
2.	Kopmaba	July 1997	Urban	217	Yes
3.	Anugerah	November 1997	Urban	69	No
4.	Mitra Sejahtera	February 1998	Urban	231	No
5.	Mitra Umat	No activities	Urban	30	No
6.	Mitra Mandiri	March 2000	Urban	88	Yes
7.	Mitra Wargi Saluyu	November 2000	Urban	32	Yes
8.	Surya Mandiri	July 1999	Urban	20	Yes
9.	Dulang Perak	November 2000	Urban	23	Yes
10.	Multi Usaha	November 1998	Urban	N A	Yes
11.	Setia Kawan	November 2000	Urban	N A	No
12.	Tatali Wargi	January 1995	Urban	426	Yes
13.	Mega Prima	February 1999	Urban	56	Yes
14.	Paguyuban Warga	July 1983	Urban	60	No
15.	Koprima	November 2000	Urban	22	No
16.	Cibangkong Sebelas	November 1998	Urban	179	No
17.	BMW Sumadang	July 1998	Rural	102	Yes
18.	Batulonceng	May 1998	Rural	30	No
19.	Nurul Amal	April 1998	Rural	62	Yes
20.	Kowardes Berkah	November 1999	Rural	36	Yes
21.	Baruna Siribon	February 2001	Rural	N A	Yes

Source: LPKM

§ 4.2 The entrance of new institutions

As mentioned before in April 2001 there were 21 microfinance institutions affiliated with LPKM, but in less than four months this number increased with more then one third: to 29 institutions at the beginning of July 2001. Through all kinds of ways, starting or already existing institutions contact LPKM. New institutions sometimes simply apply at a training or LPKM receives a letter with a proposal to become a member.

When a microfinance institution wants to become affiliated to LPKM, it must meet certain requirements[7]. The first requirement is that it must provide data to LPKM. These data consist mainly

[7] The staff at LPKM is relatively strict in the rules they apply; by being so and also by maintaining a good database they prevent that the money falls in the wrong hands.

of personal information on its members, the activities and services the institution provides, capital and background information of all staff members of the institution. The microfinance institutions must also deliver a monthly financial report to LPKM (balance sheet and income statement). To monitor the microfinance institutions, but also to give information on whether the staff needs help accounting. At the end of each year all microfinance institutions have to present a report called RAT (Rapat Angota Tahunan). When a new institution is approved, it has to introduce itself at a meeting, but often everybody already knows about the existence of the new institution.

In the future every new microfinance institution needs a recommendation by at least three other microfinance institutions before the admission is approved. The three existing institutions judge the new institution by looking at the skills, motivation and seriousness of staff members. In addition, the business proposal will be scrutinised. In case the ‘new’ institution does not repay the loan, the three microfinance institutions recommended the newcomer are held responsible. The sanction does not mean that the three microfinance institutions need to pay the loan back, but they will be excluded from future loans. LPKM welcomes this initiative because there is simply not enough money to redistribute. Therefore the recommendation letter is perceived as an effective selection criteria; also it shows that the other microfinance institutions are partly responsible.

A rational problem that will arise as a result of this new rule, is that the microfinance institutions will be somewhat reluctant to give a letter of recommendation to new microfinance institutions. Hence, when there are more microfinance institutions eligible for a loan, this will mean that there is less money available for each individual institutions. This problem is enhanced by strong signals that point out that LPKM has a limited amount of money. Whether this new procedure will make existing institutions reluctant has to be awaited. Furthermore, this influences the extent of co-operation and dependence between the microfinance institutions, which distinguishes it from other microfinance programmes.

§ 4.3 Staff of microfinance institutions

The Indonesian law obligates microfinance institutions to have a minimum staff of three people: chief, secretary and treasurer (see also subsection 4.6). The members of the institution elect the chief of the institution. In practice however, three persons are not enough to run a microfinance institution properly. For the affiliated institutions the average number of staff members is five. Every institution also has an advisor. This advisor does not deal with daily activities but gives advice on how to deal with certain problems and the management of the institution. The advisor can be a formal or informal leader or a member. For instance, the advisor of three institutions (BMW Bandung, Mitra Sejahtera and Kopmaba) is the head of LPKM, Mr. P.C. Suroso.

Later on, a creditor team can be formed to assist the staff of the institution. At this moment there are four institutions (Kopmaba, Tatali Warga, Mitra Sejahtera, and BMW Bandung) that have a creditor team. In the future LPKM wants every affiliated microfinance institution to have a creditor team. This team consists of three people, who can be members of the institution. They report on the business proposals from members to the chief of the institution. The decision for granting a loan is not solely based on the opinion of the credit team; their opinion is only taken into consideration. The creditor team also monitors the loans to members and reports when a member is late with his repayment and asks the staff to visit him. Other activities of the creditor team are identifying the purpose of the loan, monitoring some of the small-scale entrepreneurs and crosschecking friends of the members to see whether the loan is used according to the proposal.

§ 4.4 Reward for the staff

As mentioned before, one of the striking differences with the organisation of other microfinance institutions is the arrangement concerning the remuneration of the staff of these microfinance institutions. All the institutions are independent, so if they make more profit, there is more money to pay salaries and the to distribute money in the form of loans. A well-designed incentive scheme rewards staff behaviour that benefits the microfinance institution and punishes behaviour that results in increased risk or a loss to the institution. Therefore, it is crucial that LPKM understands what type of behaviour will lead to which results, so that it can help to design an incentive scheme in such a way that the microfinance institutions' productivity and profitability increases. It is also important to bear in mind the effect different incentive schemes will have on clients and their needs. Moreover, one should not overlook the influences of the reward system on the morale of the staff drawn in by the programme's social mission, which can lead to management challenges. These are issues that certainly need more attention, when the institutions are more established.

At an institution all staff members start as volunteers. Table 4.2 shows that, 53 per cent of the staff members receives no salary. From these people, 22 per cent works voluntarily at the microfinance institution, but none of them would like to continue working voluntarily. Normally, staff receives only a salary when the institution starts collect interest, which can take more than six months. But often the staff receives a salary after three or four months. Table 4.2 shows that this salary mainly depends on the performance of the institution, and 68 per cent of the respondents would like to be rewarded like in that form.

The salaries are paid by the instalments, but only after all expenditures and loan repayments to LPKM have been made. The institutions make use of the so-called targeting system: if the staff members do not collect the instalments, they do not receive a salary. Sometimes when a microfinance institution after a long period still cannot pay a salary to its staff, LPKM or Mr. P.C. Suroso will pay the salary. This is done to make the institution financial stable. When an institution makes a profit and is able to pay a salary, it is free to decide what amount they should be paid as a salary. LPKM advices on the height of the salaries. Until now there have been no real problems with the payment of salaries.

Table 4.2 Reward for staff of microfinance institution

(1) How are you rewarded for your work at the microfinance institute?	**(%)**
No salary, but voluntary	22
No salary, but in the future I will receive a fixed salary	6
No salary, but in the future I will receive a salary	25
Salary based on the performance of my institute	0
Fixed salary plus based on the performance of my microfinance institution	29
Salary based on performance of my microfinance institute	13
Other	5
(2) How would you like to be rewarded for your work at the microfinance institute?	**(%)**
No salary, but voluntary	0
No salary, but in the future I would like to receive a fixed salary	7
No salary but in the future I would like to receive a salary	16
Based on the performance of my institute	0
Fixed salary	2
Salary based on performance of my microfinance institute	68
Other	7
(3) How many hours a week do you work at the microfinance institute?	**(%)**
Between 0 and 8 hours	61
Between 9 and 16 hours	12
Between 17 and 24 hours	9
Between 25 and 32 hours	7
Between 33 and 40 hours	2
Between 41 and 48 hours	9
More than 49 hours	0

Respondents: 65 staff members

The salaries of course also depend on the hours worked at the institution. Not many staff members work full-time at the institution; often they have another job somewhere else. The table shows that 61 per cent works less than eight hours at the microfinance institution and only 9 per cent works more than 41 hours.

§ 4.5 New members

This section explains the procedures and the requirements to become a member of a microfinance institution. Chapter 6 deals with the outreach of the microfinance institutions, while in this subsection the general application procedure is addressed. When somebody wants to become a member of a microfinance institution he or she has to announce this at the institution. From the respondents 34 per cent find out about the institution from his friends or neighbours and 30 per cent directly from the staff of the institution. In a preliminary conversation the staff often explains the process of application and the activities of the microfinance institution briefly. The applicant has to fill in an application form (Formulir Keanggotaan), stating his name, date of birth, address, occupation, area of occupation, salary, education, skills, work experience, and the reason for applying. The most common reason people apply is because they need a loan (36 per cent). The low interest rate is the second reason people want to become a member of an institution (see table 4.3).

Table 4.3: Members

(1) How did you find out about microfinance institution	**(%)**
From friends	23
From staff visited my house	16
Went to institution and asked the staff	14
From neighbours	11
Asked around	9
From other members	7
Through mass media (radio/television)	7
From family	5
Through meeting/training from microfinance institution	5
From chief of area	2
Through other organisation	2
(2) Reason applied	**(%)**
Needed the loan	36
Low interest rate on loan	34
Training at institution	16
Could not get loan elsewhere	6
Social activities	4
Other	5
(3) Intended purpose of the loan	**(%)**
To run the existing business	34
To grow and to expand the existing business	32
For expenditure related to family	14
To start for the first time a business	12
For medical expenses	4
For an emergency	3
For social ceremonies	1

Respondents: 63 members

The Pengurus (chief, secretary and treasurer of the institution), at some institutions together with the creditor team, checks all the provided data. *The Pengurus* also checks whether the applicant is not a member of another institution or has outstanding loans somewhere else. However, it is quite difficult to check whether people have outstanding loans at other moneylenders. Much of the analysis of the new member is based on trust and interpretation by the Pengurus, because according to the respondents 23 per cent of the staff members looks how serious and motivated the new member is. Moreover, *the Pengurus* asks the member whether he will obey the rules, and the institution makes a business analysis (done by both 11 per cent from the staff respondents). Also non-measurable factors such as the character of the applicant and his honesty are factors influencing the decision of allowing the applicant to become a member. Besides this, the opinion of other members (4 per cent), colleagues (2 per cent) and neighbours (2 per cent) are considered in the decision.

When a new member has been analyzed, the staff notifies him. To become a member he has to pay a one-time entrance fee of Rp. 5,000-10,000 administration costs. In return the new member receives a bankbook in which his loan status and savings are recorded. After three months the new member can apply for a loan, because first he has to save at the institution. The factors taken into consideration before granting a loan are: business proposal (34 per cent), knowledge of the new member (24 per cent), opinion of other members (19 per cent) and opinion of neighbours (11 per cent).

§ 4.6 Procedures for microfinance institution to get a loan

This section outlines the procedures for the microfinance institutions to get a loan from LPKM and the requirements the members have to meet before becoming eligible for a loan. Financial intermediation is one of the categories of services provided by LPKM and their micro enterprises; the social services were described in section 3.3. This description will shed light on the more important parts of this paper and the implications of these procedures.

Every existing microfinance can go to the training provided by LPKM, but in order to be eligible for a loan the microfinance institution has to meet the following six requirements:

1. have at least 20 members;
2. have at least three staff members;
3. have an office address;
4. have a financial report;
5. build capital;
6. must exist for at least three months.

First, every microfinance institutions must have a minimum of twenty members. These members do not necessarily have to be borrowers or savers, they just have to be members. Second, the staff of the microfinance institution has to consist of three people: a chief, secretary and a treasurer. These two obligations are government rules or guidelines. Third, the institution must have a fixed office address. Fourth, the institution must hand in a financial report every month to LPKM. Fifth, the institution must build some capital and the last requirement is that the institution must exist for at least three months in order to build capital, before LPKM extends a loan. The precise amount of required capital depends on the total amount of savings and the number of borrowers. There is no government regulation concerning the minimum capital requirements. The standard path to raise capital is to collect savings of potential borrowers. It is possible to get a second loan while there is still a loan outstanding, however this procedure does not apply to the first loan granted to a microfinance institution.

LPKM only grants loans to the microfinance institutions, which are responsible for returning the interest and principal. The annual interest rate LPKM charges is four per cent nowadays. In the past

LPKM had different interest rates for different loan amounts. For loans between Rp. 0–10,000,000 the interest rate was 6 or 8 per cent. The precise rate depends on the negotiations and the financial performance of the microfinance institutions. If the loan extended is larger than Rp. 10,000,000 the interest rate drops to 4 per cent. The LPKM employee rationalised this by saying that otherwise the interest payment is too much of a burden on the financial position of the microfinance institutions. Loan repayments must be made on a monthly basis. In general the loan term is between one and three years, depending on the negotiations and whether or not the microfinance institution thinks it will be able to pay back the loan. The loan amount is normally not bigger than Rp. 2,000,000. This amount can only be bigger, if the microfinance institution has a good reputation and solid financial reports, but the loan term cannot be longer than three years. The loanterms and amounts are unilaterally set by LPKM.

Chapter 5 Asymmetric information

In the literature much attention is paid to group lending to alleviate the problems caused by asymmetric information. In line with the literature (as described in chapter 2), we focus on the use of group lending mechanisms among other things. This is however not the only mechanism that is available to make borrowing to people who are excluded by formal banks a success. LPKM uses regular meetings (section 5.2 and 5.3), dynamic incentives (section 5.4) and progressive lending to deal with the problems caused by asymmetric information.

§ 5.1 Group lending

As mentioned in chapter 2, group lending contracts generate several benefits. There are mechanisms at work that allow these programmes to generate high repayment rates from low-income borrowers without requiring collateral. However, not every microfinance institution makes use of group lending contracts that feature joint liability. For example, new programmes in Russia and Eastern Europe have demonstrated the advantages of employing individual-based contracts instead of using only group lending contracts. Also, Bank Rakyat Indonesia does not use group lending mechanisms. And, unlike many other microfinance programmes, the BRI requires the individual borrowers to pledge collateral. As a result, the poorest borrowers are excluded. The microfinance institutions affiliated with LPKM make incidental use of group lending contracts. Most of the programme is based on individual contracts, with individual liability.

§ 5.1.1 Group lending by the microfinance institutions

Group lending contracts only occur at three microfinance institutions: BMW Bandung, Kopmaba and Cibangkong Sebelas. The size of the first loans provided by the microfinance institutions to their members is often small. When the borrowers have proven their creditworthiness and have established a long-term relation, the actual amount they can borrow may become bigger. If a borrower applies for a loan that is more than Rp. 15,000,000, the member is obligated to form a group that consists of at least five members. This principle is the opposite of many other programmes elsewhere, since in general members have to form groups in order to get a “small” amount of capital. This rule can withhold wealthier borrowers. Therefore, Bancosol and the Grameen Bank have abandoned group lending and now use individual loan contracts for their richer and most-established borrowers. The group lending contracts are especially used for becak drivers (paddlecab drivers) and farmers. This will be discussed in more detail in subsections 5.1.4 and 5.1.5.

§ 5.1.2 Group formation

In short, the use of group lending potentially works better than other financial contracts, because group members have superior information on one another and can impose non-financial sanctions on one another. Should the group be initiated by the microfinance institutions or can the members form their own group? It appears that screening is more effective within groups that are formed by their own than within those groups that depend interference by the institution. The degree to which group members know each other and interact on a regular basis is of importance in this context. When potential members do not know each other initially, it would take considerable time for people to perceive just how honest and trustworthy others are in related group lending contracts. Hence, group formation is a critical component of successful group lending. The process of the formation of groups influences the structure of the group and therefore conditions its consequent conduct and performance, along with the characteristics of the programme and the group’s community. We do not attempt to model the stages that lead to the formation of groups or the consequences of the final outcome of this process on the repayment performance.

The meetings between the staff of the microfinance institutions and their members can function and do function as a means to learn more about the other (group) members and they help to increase group solidarity. As is shown in table 5.1, in most cases the members can choose their other group partners themselves, and usually they form groups with friends. Therefore, it seldom happens that they do not know their other group members well. According to the data from the members of the institutions, the other members of their group are friends (64 per cent), relatives (29 per cent) or neighbours (7 per cent). This is because in 92 per cent of the cases the people can choose the other group members themselves. Members are very careful about whom they admit into their group, given the threat of losing access to future credit or the possibility of having to pay off someone else’s loan with their own savings. Hence, rules concerning group formation are a crucial component of successful group lending.

The loans are made to the individual borrower, but the group as a whole is responsible for loan repayment. The rule states that if one member of the group ever defaults, all others in the group are denied subsequent loans. This rule is initiated by LPKM and is used by all affiliated microfinance institutions. Because of this rule, most members (62 per cent) responded, chose the other group members mainly on the basis of their good reputation (creditworthy and character of the member). When group members are involved in the same economic activity, the cost of monitoring can decrease. While this argument appears to be justified, there are circumstances in which this is not the case. The ability to obtain relevant information on others does not solely depend on the homogeneity in occupation. There are more ways to gather information. While it is too early to asses the success of group lending using this methodology in this particular context, an open mind to allow groups to be formed voluntarily among different professions is valuable, thus paying attention to the factors that influence access to information and the way information is transmitted in the social system of Indonesia.

Table 5.1 Group formation

(1) With who did you form a group to get a loan?	**(%)**
Friends	64
Relatives	29
Neighbours	7
(2) Could you choose the other group members?	
Yes	92
No	8
(3) If you chose the other members, why did you choose those people?	
They have a good reputation	62
We get along well	13
We are neighbours	11
Others have specific skills for occupation	7
Group formation is based on where they live	7

Respondents: 63 members

§ 5.1.3 Group arrangements

From the group members 92 per cent responded that their group often meets and has formulated rules (table 5.2). The most important rule (42 per cent) between members of a group is that everyone must pay the instalments on time. Other rules made are less easy to enforce and more informal, like agreements about honesty, discipline and trust. Besides rules, all groups have constructed a savings scheme. An example of a savings scheme will be given in subsection 5.1.4.
In a group lending contract only 8 per cent of the participants never had a late repayment. This is very low and indicates a relative bad performance of the group. However, in most cases when a group member had difficulties the group as a whole (75 per cent) offered help to the member (see table 5.2). Second, a person of the group (17 per cent) and third the respondent himself (8 per cent) offered help to the member in need. According to the respondents the help offered to the group member who had difficulties repaying the instalment, was mainly financial; sometimes business support was offered (see table 5.2) - probably because many of the group members are in the same economic activity. Due to the joint liability of the group, the obligation to help the group member in need is very high. Table 5.2 also shows that participants monitor other group members well. Often, the group as a whole (in 60 per cent of the cases) or an individual of the group (26 per cent) addressed the group member with the problem.

Besides the sanctions for the group as a whole, the group itself has sanctions for the group members. For instance, a reminder and a fine will be given to the member that repays late, and in the worst case the group as a whole can dismiss a member to avoid further problems.

Table 5.2 Group arrangements

(1) Does your group meet regularly?	**(%)**
Yes	92
No	8
(2) Did your group make rules?	**(%)**
Yes	92
No	8
(3) What kind of rules are these?	**(%)**
Repay loan on time	42
Be honest	17
Save	8
Be disciplined	8
Trust each other	8
Follow rules of institution	8
Informal agreements	8
(4) Does your group have a savings scheme?	**(%)**
Yes	100
No	0
(5) Was there any member in your group who had problems repaying his instalment?	**(%)**
Yes	92
No	8
(6) Did he receive any help?	**(%)**
From the group as a whole	75
From somebody else from the group	17
From myself	8
(7) What kind of help was offered to the person?	**(%)**
Financial	83
Business	17
(8) Who addressed the person of the group when he could not pay the instalment?	**(%)**
The group as a whole	60
Myself	13
Somebody else from the group	13
The chief of the microfinance institution	7
The staff of the microfinance institution	7

Respondents: 63 members

§ 5.1.4 Group lending for becak drivers

An exception to the rule that a group has to be formed for amounts over Rp. 15,000,000, are the loans provided to becak drivers. The becak drivers also have to form a group for loans less than this amount. The loan amount for the becak drivers is somewhere around Rp. 2,500,000 and the loan term is approximately eighteen months. The loans to the becak drivers give them the opportunity to buy their own becak. The staff of the institution not only grants the loan, but also accompanies the borrowers to buy the assets. There is a mutual benefit to this: the staff ensures that the borrowers do not use the money for other activities (for instance, gambling), and the borrowers are sure that they pay a normal price for the becak. Thus, there is a controlling process from both sides. When the becak drivers repay all the instalments, the becak becomes theirs. At this moment the becak drivers rent their becak, but they will never have their own. By giving them the opportunity to become the owner of the becak gives them selfesteem and more incentives to work.
One of the reasons for the microfinance institutions to use group lending for becak drivers is because they are regarded as very risky borrowers. By making use of group lending, the cost of screening, monitoring and enforcement are to a large extent transferred to the group members. This makes it possible for the institution to reach more members and also the more risky clients, even in the face of asymmetric information. Especially the becakdrivers have excellent knowledge about who is a reliable creditor and who is not. They spend all day together, and therefore they are very capable of choosing the other group members.

A big difference with other microfinance programmes is that the institutions charge the same interest to becak drivers as they do to other borrowers, while the becak drivers belong to a category that can be considered as very risky: the becak drivers work on the streets all day and often have to wait long for a customer, so in their spare time they like to gamble. This is one of the reasons why they have to pay the instalments every day. Every day the group members have to pay Rp. 2,000, from this Rp. 1,500 is interest and principal, and the remaining Rp. 500 is the amount they have to save each day. This amount is quite a burden for the becak drivers, since their daily income usually is between Rp. 4,000 and 10,000.

§ 5.1.5 Group lending for farmers

Another group lending system, only used by the microfinance institution Kopmaba, is for buying a cow. Members could sign in if they were interested in a loan, that can be used only to buy a cow. 17 members in total were interested, but because the price of one cow is approximately Rp. 3,000,000 and the funds of the microfinance institution are limited, the staff of Kopmaba and LPKM tried to look for a solution that would benefit as many members as possible. They came up with the idea to form one large group of these 17 members. There was only money to provide a loan to three members. The decision was made to let a lottery pick the families who would get the first loans. The other group members would receive a loan after the first members successfully repaid their loans. At worst, they had to wait several years for a loan, but all group members agreed with the lottery. The term of the loans was three years and the instalment was Rp. 1,000,000 per year. After one year, when the three members repaid their instalments, a new loan to buy a cow could be granted to another group member. The cow is an individual asset, and the loan is provided to an individual. To repay the loan the members can use the revenues from the sale of young cows and other products. If the member cannot repay the loan, he will not receive a new loan in the future and the cow will be given to the next member. Thus, the cow is used as a collateral. The land of the member is also used as a collateral. For instance, if a member secretly sells the cow, the institution can claim the land of the borrower, but this has never happened. It seems that this group lending initiative for a cow is working, but the duration of the project is too long and the impact is too little to copy the system to other areas.

§ 5.1.6 Dilemma

There is an inherent dilemma in the design of the group lending contracts used by microfinance institutions. The microenterprises usually have very little start-up capital. Most urban enterprises operate on short-term planning cycles, often daily or weekly. This is also evident from the loans outstanding at the microfinance institutions: short-term finance, in quite small amounts, what is most needed. As the businesses of the members develop they need larger loans. This is where a problem arises: from a financial perspective, a successful microfinance institution will in general have high repayment rates[8]. As a microfinance institution develops, its client base demands larger loans. This follows from the use of progressive lending and the development (expansion) of the enterprises of the members. But there are limitations to group lending contracts, which led Russian and Europe programmes to focus on individual lender-borrower contracts instead (Aghion and Morduch, 2000).

The staff of LPKM told us that in the future they want to address group lending contracts for farmers. This can mean that they alter the design or stop loans based on groups. Until now LPKM and the microfinance institutions are not pleased with the group lending contracts. The precise reason for this is unknown.

§ 5.2 Meeting members and staff

A few times a year the staff of the microfinance institution organises a meeting for all its members. The number of organised meetings often depends on the needs of members and differs per institution. The purpose of this meeting is to strengthen the social cohesion, to profit from people's natural disposition to avoid social stigma as an incentive to repay loans and to discuss all kinds of problems. This can be associated with the handing out of all kinds of awards to its members during a meeting between the members and the staff of Kopmaba. Awards were given to the best borrower, best group leader, best group member and the entrepreneur with the best management. The three main topics of the meetings were the financial report of the institution, the regulations and the late repayments. By discussing repayments by individual members, the institution transfers part of the costly monitoring

[8] Despite the success of microfinance institutions in their ability to achieve financial sustainability. The "successful" achievement of financial sustainability may involve large costs in terms of borrowers, socio-economic impoverishment.

effort, normally incurred by the institution, to the borrowers. However, this peer monitoring is not as intense as with group lending. The monitoring effect from public discussion of late repayments at meetings is enforced by the fact that all members know each other well and live close to each other. According to the data from the members questionnaire, 12 per cent knows the other members very well and 80 per cent knows the other members well[9].

The meeting with the members can be an elementary source of information from which the staff can get information on potentially delinquent borrowers, and the assembly can be used as an instrument to create pressure. Moreover, meetings can facilitate education and training in a wide range of areas. Another advantage of these meetings is that the transaction cost of lending small amounts can be reduced for LPKM as well as for the microfinance institution. The meetings are also used to collect the instalments and to hand in new loan proposals, so it is an efficient way to avoid transportation costs. Finally, because the target group of microfinance institutions have by definition little experience with banking, the needs and comfort of the clients can be met by encouraging them to approach the microfinance institution as a group. For all these different reasons the meetings between the members and the staff are important.

Another function of the meetings is voting. Every attendant at the meeting receives a voting right. In 77 per cent of the cases the staff of the institution decides the topics of voting. The two main topics of voting are regulation of the microfinance institution and plans to develop the institution. Other topics of voting are for instance the members of the staff, obligations for members and election of profit distribution (Sisa Hasil Usaha). A special meeting at the end of the year is organised to present the annual report, Rapat Angota Tahunan, to the members. This report contains information concerning the loans outstanding, total members, the distribution of next year's profit, and several financial issues. For instance, the institution can decide to use the profit to distribute to its members or invest in the institution. It is good to see the contribution of members by voting, but according to the staff respondents, 95 per cent of the microfinance institutions use the votes of the members only as a recommendation and no one uses it as a real obligation. This could indicate that the role of voting is not as great as it might be.

The attendance at these meetings differs per meeting. Members often have other more important things to do; for example work or some kind of emergency makes it impossible for them to attend the meeting. However, the staff of the microfinance institution does not invite every member to the

[9] While LPKM only indirectly interacts with the borrowers of the microfinance institutions, sometimes there is an exception. They never address the clients of the microfinance institutions without consulting and without the approval of the microfinance institutions, since that would be regarded as impolite. If microfinance institutions have substantial difficulties with one of their members, for instance regarding the repayment, LPKM can act as an intermediair and hopefully they can reach an agreement.

meeting; 86 per cent of the respondents says that not every member is invited to the meeting. Attending a meeting brings along opportunity costs, because the time spent at the meeting cannot be used for working. While the opportunity cost of time is higher for the rich, meetings may also drive away the poor. The height of the costs of attending in a meeting depends on a number of factors. First, the distance members have to travel to come to the meeting place. For 72 per cent of the members the distance from the members' house to the microfinance institution is less than 500 meters. This indicates a relatively low time cost of participation, but 12 per cent has to travel more than 3 kilometres. The average distance from the members' home to a meeting place is 7.6 kilometres on average, with the highest distance being 100 kilometres and the lowest of 10 meters. Especially in the rural area the distance from the members house to the institution is great. The length of the meeting is the second factor influencing the time cost of participation. The duration of the meeting between members and staff is in most cases (84 per cent) no longer than two hours. The average meeting time is 115 minutes, and the average appropriate meeting time according to the members' respondents is even longer, so members are willing to bear the cost, which indicates an appreciation of the meetings.

§ 5.3 Meeting staff and LPKM

Every month a meeting between the staff of all affiliated microfinance institutions and LPKM is organised. Often, it is difficult to pick a day and an appropriate time for the meeting, because of the large number of people invited. The purpose of the meeting is to discuss problems the institutions face and to discuss the financial reports. At the beginning of the meeting the staff members of the institutions can list topics or problems they wish to discuss during the meeting. The topics discussed at the meeting in June 2001 were:

- how can an institution make new members;
- how to deal with administrational problems;
- low attendancy at meeting between members and staff of institution;
- how to get funds;
- which criteria should an institution use to distribute the money;
- unawareness of the other services provided, such as training;
- how to make a new proposal to receive a loan from LKPM;
- how to cover costs, the interest rate being much lower at formal banks;
- how does LPKM deal with late repayments of the institutions;
- what if LPKM lacks funds to distribute among the institution.

Later on at the meeting the staff of LPKM tried to answer these questions. For instance if an institution has problems with the administration, the staff from other institutions try to make a positive contribution to the solution of the problem. Perhaps they faced the same problems and they can explain how they solved it. Support and assistance is not only offered by LPKM, the microfinance institutions also try to help each other and share experiences. Thus, the discussions are always very interactive.

Besides these topics provided by the staff of the affiliated institutions, there are some topics that are fixed and therefore discussed at every meeting. At the meetings the microfinance institutions are informed about the financial performance of their colleagues. This is explicitly done at the beginning of the assembly. The staff is forced to run their microfinance institution properly, to avoid that they will be embarrassed in front of their peers[10]. This stimulus is at this moment quite forceful, since the financial resources available are scarce.

In the future LPKM wants to rely more on peer pressure; staff of the microfinance institutions will visit each other to exchange advice and recommendations[11]. There is a clearly pattern of enhancing the co-operation is visible.

Every year the best institution receives a reward for its performance. At the meeting in June 2001 LPKM handed out an award to the best institution, Mitra Sejahtera. This was mainly based on their administration, financial report, and repayment. They receive a trophy and a certificate. The attendance of the meetings varies; at the meeting in April only 62 per cent (13 of the 21) of the affiliated institutions attended and at the next meeting 75 per cent institutions attended. As mentioned before, attending a meeting brings along opportunity costs. It shows that the average distance from the staff members' home to the meeting place with LPKM is 37 kilometres, with a maximum distance of 90 kilometres and minimum of 10 metres. Also, almost every staff member has to make use of public transportation, which takes more time to travel. The cost of travelling is to some extent paid for by LPKM. The length of the meeting between the staff of the institutions and LPKM is on average 239 minutes.

§ 5.4 Dynamic incentives

Dynamic incentives are often used by microfinance institutions as a tool to enforce repayment. The institutions affiliated with LPKM use the threat of losing new or additional loans as a mechanism to enforce repayment. Table 5.3 shows that in most cases when a borrower could not repay the instalment on time, the institution banned the delinquent borrower. The formal policy is that borrowers are shut off from future credit when they are three times late with their payment.

The above description is the formal transcript, it is difficult to judge how flexible or strict the microfinance institutions follow this policy[12]. To ensure timely repayment LPKM visits the microfinance institutions and inflicts pressure on the microfinance institutions. The impression we got was that LPKM has a flexible attitude towards the microfinance institutions. This policy is recommendable, since it allows LPKM to adapt to new situations and conditions in order to build a

[10] In Indonesia people want to avoid situations and circumstances that make them feel *malu* (embarrassed).
[11] A consequence of this intensified cooperation, was the merger between Batalungceng and BMW Bandung.
[12] After the financial crisis the terms and conditions were less strict.

long-term sustainable relationship with the (new) microfinance institutions. For instance, if a micro credit enterprise faces difficulties, it can obtain more time if there is a valid reason.

Table 5.3 Dynamic incentives

(1) Did the staff of the institution come to you when you could not repay the instalment?	**(%)**
Yes	92
No	8
(2) What did the microfinance institute do when you could not repay the instalment on time?	**(%)**
Banned me from further loans	32
Made a new loan agreement	23
Gave me a remainder	18
Gave me a fine	12
Made me pay double the next month	4
Visited me and asked for reason	4
Other	9
(3) If you pay all instalments on time, do you think you can get another loan?	**(%)**
Yes, definitely	66
Probably	23
Probably not	5
Do not know	6
(4) If you have successfully repaid a loan in the past, did you get another loan?	**(%)**
Yes	90
No	7
Depending on need	3

Respondents: 63 members

When the staff receives signals that a borrower faces difficulties, they visit the member and try to find a solution. However, the microfinance institutions have specific rules concerning late repayments. The basic rule can best be explained with an example. This month a borrower is due Rp. 100,000. Even if the borrower is one day late with the payment, the fine is two per cent of the Rp. 100.000. After one month the penalty rate is increased by 2 per cent to 4 per cent, this means the fine is 4 per cent of the first Rp. 100,000 and of the amount due the next month. When the delinquent borrowers pay their fines, they are eligible for another loan but they certainly do not have priority. Another sanction issued by the other members is that at the end of they year they vote on which problematic borrowers are candidates for terminating of their membership. Of course, these borrowers can defend themselves. Generally, this is the policy, but the precise level of the penalty rate differs according to the agreement between the microfinance institutions and their members.

The members think that they will receive a new loan if they repay the old one on time and without problems. Only 5 per cent of the respondents thinks that he will probably not receive another loan in the future (see table 5.3). The staff of the institutions responded that the members would definitely receive another loan if they pay all the instalments on time. It shows that 90 per cent of the respondents did indeed receive a new loan after repaying the first one. When a member repaid all the instalments on time but did not receive a new loan, this was due to the lack of funding at the microfinance institution, or the members ask for an amount that was too large for his individual credibility.

This threat, dynamic incentives, can only be meaningful if members think or expect the microfinance institution is willing and able to strictly deny loans to clients who do not repay. While the loan size depends on the amount of savings among other things, microborrowers can obtain a larger loan when they repay their old loan (progressive lending). Microfinance institutions should be careful about granting loans to already problematic borrowers, since this can harm the discipline of even good borrowers. The microfinance institutions as well as LPKM must follow a policy that states that delinquent borrowers will not be eligible for a new loan and both must be willing to communicate this to the clients.

The threat to exclude a defaulter from future credit is less effective if individuals can simply move to another moneylender. Competition among the microfinance institutions belonging to LPKM and competition between other programmes can diminish dynamic incentives and undermines the repayment rates of both programmes. Co-operation with the other microfinance programmes can therefore be mutually beneficial, since the objective is to reduce poverty and not to make a profit. To prevent the switching of members LPKM has ordered that a member can only be affiliated to one microfinance institution. The strength of this incentive is also influenced by how much borrowers care about future credit availability and whether they prefer moneylender to others. Thus, this threat depends heavily on the alternative sources of credit being very expensive or non-existent.

Chapter 6 Outreach of the programme

A target market is a group of potential clients who share certain characteristics, tend to behave in similar ways and are likely to be attracted to specific combinations of products and services (Morduch, 1999). A microfinance institution can identify its target market by looking at the characteristics of the potential clients. In this chapter we look at four characteristics of the members that influence the impact, design and performance of the programme: poverty level, gender, geographic focus, and ethnicity and religion.

§ 6.1 Poverty level

The extent to which microfinance focuses on the poor depends among other things on whether the height of the interest rate will deter the poor**.** The interest rate annually charged by the institutions is approximately 24 per cent. Bank Rakyat Indonesia (BRI) provide loans that tend to be larger (and thus less focused on the poor) at a commercially viable rate of 34 per cent per year (Park and Chen, 2001). The rates of commercial banks are even higher. The microfinance institutions compete with the black market (40 per cent per year) by combining lending services with other non-financial services and by charging a lower interest rate. In this context it is important to keep in mind that Bank Indonesia now expects inflation to be between 9 and 11 per cent in 2001 (World Bank, 2000). But while subsidising interest rates can improve targeting in theory, in practice charging interest rates that are too low makes the loans attractive to the rich. One way to circumvent this is to exclude richer households on the basis of eligibility requirements. These very low interest rates compared to official interest rates have made the loans also attractive for enterprises and revenue-generating projects. The distributors and leader of the microfinance institutions are sensitive to nepotism, making it difficult to implement eligibility rules effectively.

When members of the institutions affiliated with LPKM were asked what the highest interest rate per month was they are willing to pay, the average response was 2.44 per cent. The average rate they felt they could pay was 2.26 per cent per month (see table 6.1). The average loan amount is Rp. 834,375, but 93 per cent of the respondents said they would not be willing to pay more interest for a larger loan.

Table 6.1 Reaching the poor

(1) What is the highest monthly interest rate you are willing to pay?	**(%)**
0.83%	8
1.5%	4
2%	45
2.5%	2
3%	27
3.5%	8
4%	2
5%	4
Average 2.44%	
(2) What is the highest monthly interest rate you are able to pay?	**(%)**
0.83%	8
1%	2
1.5%	2
2 %	55
3%	25
3.5%	8
Average 2.26%	
(3) What amount did you receive as a loan?	(%)
< 250,000	26
250,000 – 500,000	33
500,001 – 1,000,000	19
1,000,001 – 1,500,000	10
1,500,001 – 2,000,000	5
2,000,001 – 2,500,000	2
> 2,500,000	5
Average Rp. 834,375	
(4) Would you be willing to pay more interest for a larger loan amount?	**(%)**
Yes	7
No	93
(5) Do you have any outstanding loans at an institution than at your microfinance institution?	**(%)**
Yes	49
No	51
(6) What are the sources of these other loans?	**(%)**
Family	58
Formal bank	21
Informal agent	11
Friend	5

Insurance office	3
Work	3
(7) If there were no microfinance programme, would you still undertake the project?	**(%)**
Yes	84
No	16
(8) If you still undertake the project, would the scale be the same?	**(%)**
Yes	75
No	21
Maybe	4
(9) If yes, where would you get the funds?	**(%)**
Savings	48
Borrow from informal sources	30
Borrow from formal bank	11
Both sell product and borrow	4
Family	4
Other	3

Respondents: 63 members

If we look at how many of the respondents have a loan somewhere else than at the microfinance institution, we see that this is the case for 49 per cent. This could mean that these members borrow somewhere else to repay their loan to the microfinance institution or vice versa. From this 49 per cent, 58 per cent has a loan outstanding at family, which is often not seen as a 'real' loan. Furthermore, 21 per cent has a loan at a formal bank, this is remarkable because normally (the poorest of) poor are excluded from formal bank, because of the collateral requirement and the higher interest rate (see table 6.1).

Table 6.1 shows that many members would still undertake the project (84 per cent) at the same scale (75 per cent), even without the microfinance institution. Their funding would come from savings (48 per cent), which again could indicate that the clients these microfinance institutions serve are not the poorest of poor. Also, 30 per cent would borrow from informal sources, which are large competition to the institutions. These findings are rather peculiar, since the obvious question is, if they have savings to finance their project on the same scale, why do these members borrow from their institutions? One answer may be that they value the training and services provided by the microfinance institutions. This explanation is not completely tenable, because members can attend the education meetings even if they are not eligible for a microloan. However, these people do not have the priority of the microfinance institutions. Another suggestion is whether the clients have such a clear picture of their financial position in case they do not receive a loan from the microfinance institutions. In addition, it is well-known that people put money from different sources differently in mental accounts. This may explain partly why members do not use their savings as a financial source to finance their projects. These strange findings make further detailed examination worthwhile.

One of the informal sources members get money from is the black market. This black market can be a serious threat to the social mission of the microfinance institutions, since the loans from the microfinance institutions must bring net benefits to the poor. It is also possible that efforts to offer new credit (i.e. from the microfinance institutions) will simply substitute other credit sources and can therefore have small marginal effects. If loans from black moneylenders are substituted for loans from microfinance institutions, this will definitely have a positive effect on the welfare and well-being of the members (see section 3.4). However, it may not result in a better position for the low-income households members make use of the black market to pay off loans from the microfinance institutions. So high repayment rates are not the same as high impact. Evidence for this has been made available by other researchers. Rahman (1999) comes to the conclusion in his anthropological research that borrowers maintain their regular repayment schedules through loan recycling, the money comes from sources other than their own, which increases debt liability of individual households and leads to increased tension and frustration. On the other hand, loans from microfinance institutions must not simply crowd out credit from other sources (impact). This has crucial implications for moral hazard and the working of dynamic incentives (see chapter 2). It is possible that a negative impact takes place, because one programme siphons off the best borrowers, leaving the other moneylender with a more risky pool of clients and higher enforcement costs than before.

So good repayment rates can indicate that borrowers receive loans from another lender, which may provide better services, lower interest rates, or more appropriate terms. If this is the case, the microfinance institution should study how it can be of help to the members who live in poverty.

§ 6.2 Gender

Attention to gender is important, next to the effect on the repayment of loans. The provision of financial services directly to women aids in the process to empower women by increasing their economic position in society. Female entrepreneurs have attracted special interest from microfinance institutions, because they almost always make up the poorest segment of society, they are generally responsible for child rearing (including education, health and nutrition), and they often have fewer economic opportunities than men. Women face cultural barriers that often restrict them to the home (for example, Islamic *purdah*), making it difficult for them to access financial services. Also, they have more traditional roles than men in the economy and may be less able to run a business outside their homes.

The microfinance institutions rationale for targeting women over men, for example in Bangladesh, is based on the assumption of women's greater contribution to family welfare. The general hypothesis is that women's priority is to invest their earnings in their children, followed by other households' necessities. Therefore, lending to women and increasing their earnings brings more qualitative benefits to family welfare than the earnings of men (see also Pitt and Khandker, 1998).

But there are also other reasons why some microfinance programmes aim their efforts on lending to women. Experience has shown that women generally have a great sense of responsibility and are more affected by social pressure. Women are accepted in these programmes because of their vulnerable position. Vulnerability is understood by looking at the limited physical mobility of women and their culturally patterned behaviour (shy, passive and submissive). Women attend more group meetings, are more reliable, and are more disciplined. Men do not come to meetings, are arrogant, argue with microfinance institutions' employees, and sometimes they even threaten and scare them. This evidence comes from Rahman (1999) and he also shows that in the households of women borrowers the persons who control and use the loan and arrange instalments are in 60 per cent of the cases the men.

The decision to focus on women by some programmes has obvious reasons. The lower mobility of women may be a benefit where moral hazard is a problem. Also, where women have fewer alternatives borrowing possibilities than men, dynamic incentives will be increased. From the total members of the affiliated microfinance institutions in November 2000, 46 per cent were female (Suroso, 2001), but the information received from the members shows that this percentage increased to 57 per cent in June 2001. From interviews with the staff of the institutions and of LPKM we concluded that there is low mobility among members, especially among women. The lower mobility of members, and especially women, is caused by their marital status and their children. From the member respondents 77 per cent is married and only 10 per cent has no children. Both of these percentages indicate a low chance of moral hazard.

§ 6.3 Geographic focus

For a microfinance institution it is very important whether it will serve urban or rural clients. This decision greatly affects the development of products and services, and it should be based on both the activities characteristic of different geographical settings and the varying levels of infrastructure development in urban and rural areas. The institutions affiliated to LPKM serve the urban and the rural area. Five of the institutions affiliated to LPKM are located in a rural area and provide financial services to rural members, based on a general lack of supply of services outside urban centres and on the fact that in some countries poverty is largely a rural phenomenon (see table 4.1). Providing services to rural clients can therefore be an effective instrument to reach a large number of poor households. Most institutions were initiated by people living close to each other and their members also live in the same area. Therefore, for most institutions it was quite obvious where to locate the institution and whether to serve urban or rural clients. Also because of time and mobility constraints, microfinance institutions need services that are located close to their business and that can process transactions quickly.

§ 6.4 Ethnicity and religion

Indonesia has over 300 ethnic groups, while Java is relatively homogeneous with three main groups. Nevertheless, Java has various ethnic subregions with distinct variations in language and culture. The three main ethnic groups, each speaking their own language, are the Javanese of Central and East Java, the Madurese from the island of Madura off the northeast coast, and the Sundanese of West Java. The Sundanese form the second largest ethnic group in Java and in Indonesia. Indonesia is mainly Muslim, but Christian, Hindus and Buddhists communities also live in Java. Today the Islam is the official religion of 90 per cent of Javanese, and Islamic traditions and rituals affect all aspects of the daily life. In Indonesia and other Islamic countries there are specific banking laws for institutions that provide financial services. According to Khayat (1996), the main difference between Islamic and conventional banking products is that in Islamic banking, money cannot be treated as a commodity but must be used productively (like labour and land). Islamic banks also cannot charge or pay interest. The Muamalat Bank in Bandung is a bank that charges and pays no interest, but its clientele is from the strict Muslim community.

Even though UNPAR is a Catholic university; it is open to students and employees from other religions and ethnic backgrounds. However, providing community development services sometimes leads to resistance from the mainly Islamic community. The Islamic community is restrained to the Catholic programmes, because they are afraid that the programmes are not for community development but will change their religion. Among the staff of LPKM there are also Muslims, which makes the community less reluctant to the programmes.

§ 6.5 Types of activities

In addition to determining the characteristics of the clients served by the microfinance institution, it is important to consider the types of activities in which the target market is active. The economic sector of activities is also important, because each sector has its own specific risks and financing needs, which directly influence the choices made by the institution and the services and products provided. The main economic activity of the members is the running of small-scale businesses (51 per cent), as can be seen in table 6.2. The main activities of these businesses are food selling and selling other articles of use, ranging from cigarettes to candy. With 22 per cent housewives make up a large part of the members. Other occupations of members are: employees at large factories, teachers, farmers and, drivers of public transportation means. The intended purpose of the loan is for small-scale business (51 per cent), 34 per cent of the members uses the money to run their existing business, and 32 per cent needs the loan to grow and expand their existing business.

Table 6.2 Occupation of the members

(1) Occupation	**(%)**
Small scale business	51
Housewife	22
Employee	5
Teacher	5
Farmer	3
Driver of public transportation means	3
University student	3
Unknown	3
Other	5

Respondents: 63 members

Chapter 7 Financial perspective

§ 7.1 Funding of LPKM

While the microfinance institutions (and LPKM) can be rewarded for their social achievements in improving the lives of the poor, there is also another side to this story: the ongoing struggle of the microfinance institutions to relieve the credit constraints of the poor and at the same time contain the costs.

Since these microfinance institutions are not financially independent, they are substantially subsidised by LPKM and some of them are also financed by other sources. For the microfinance institutions the amount and the source of all the loans outstanding are presented in table 7.1. The column total loans lists the cumulative amount outstanding at the various moneylenders. Dapen is an account that belongs to two employees at LPKM, this is considered in more detail in Appendix C Funding. It is also shown that not all microfinance institutions receive financial resources from LPKM; nevertheless, they receive education and training provided by the staff of LPKM. As will be explained in the next section, mobilising savings can be an important source of financing the loans (see table 7.1). The column total Savings represents the savings of the borrowers at the various institutions, this is calculated by adding up the three separated savings accounts, grand savings, basic savings and voluntary savings respectively.

Large enterprises have to transfer 5 per cent of their profit to small-scale businesses in the form of a loan. A common complication was and still is that the fulfilment of these loan agreements is difficult to accomplish. Apparently, people see these as a gift they do not have to pay back, and there is the conviction that the loans come directly from the government, which has enough money in the eyes of the people. The interest rate on these kinds of loans differs between companies; the rate is usually between 11 and 18 per cent.

Table 7.1 Loan amounts outstanding and total savings (amounts in Rupiah)

Institution	*LPKM*	*Dapen*[a]	*Koerni*[b]	*P.C. Suroso*[c]	*Total Loans*	*Total Savings*
BMW Bandung	41,063,209	1,665,500	1,500,000	4,999,500	49,228,209	29,000,000
Kopmaba	61,254,632	1,500,000	-	-	62,754,632	44,543,700
Anugerah	-	-	-	-	0	7,216,000
Mitra Sejahtera	6,116,000	-	-	-	6,116,000	N A
Mitra Umat	-	-	-	-	0	N A
Mitra Mandiri	1,201,600	-	-	-	1,201,600	19,826,850
Mitra Wargi Saluyu	-	-	-	-	0	302,000
Surya Mandiri	-	-	-	-	0	300,000
Dulang Perak	-	-	-	-	0	N A
Multi Usaha	14,581,500	539,000	-	4,000,000	19,120,500	N A
Setia Kawan	-	-	-	-	0	N A
Tatali Wargi	13,899,800	-	-	-	13,899,800	73,542,329
Mega Prima	-	-	-	-	0	1,970,500
Paguyuban Warga	3,514,400	-	-	-	3,514,400	N A
Koprima	-	-	-	-	0	2,688,000
Cibangkong Sebelas	2,915,000	-	-	-	2,915,000	14,230,200
BMW Sumadang	18,071,500	-	-	-	18,071,500	5,256,600
Batulonceng	-	-	-	-	0	N A
Nurul Amal	1,667,400	-	-	-	1,667,400	N A
Kowardes Berkah	8,823,150	-	-	-	8,823,150	N A
Baruna Siribon	5,000,000	-	-	-	5,000,000	N A

a) Finance for educations of the staff

b) Lecturer at UNPAR

c) Head of LPKM

Source: LPKM

Kopmaba and BMW Bandung also received loans with an interest rate of 16 per cent from Pupuk Kujang, a government department specialised in fertilisers. The money was transferred to LPKM, but the institutions themselves are liable for the loan. To qualify for a loan from Pupuk Kujang, the microfinance institutions need a recommendation from LPKM. Another moneylender is Merci Corp International, which distributes funds across microfinance institutions and small-scale enterprises. LPKM gets its funding from many sources: university foundation, lecturers at the university, local government, and NGO's from Canada. Appendix C shows detailed information on the various financial sources.

§ 7.2 Savings

The microfinance institutions offer not only loans to the members, they also provide savings services. However, there are microfinance institutions that have members who do not save and therefore are not eligible for a loan at this moment. They merely join the microfinance institution for the training provided. This is possible and allowed, but during the training these members do not have priority. The institutions divide the savings into three accounts: grand savings (Simpanan Pokok), basic savings (Simpanan Wajib) and voluntary savings (Simpanan Sukarela). Some of the microfinance institutions bring their money to an official commercial bank. But this is rare, because microfinance institutions are usually short of money. If they do have financial resources, these are quickly exhausted since the money is redistributed to the members in the form of loans.

Each client when becoming a member is obligated to save a minimum amount of Rp. 5,000. This is called the basic or compulsory savings and the amount is the same at every institution. These savings represent funds that must be contributed by the members, and they are one of the conditions for receiving a loan. This account can best be considered as part of a loan rather than a savings product, since a member cannot appeal to this fund in difficult times and these funds are closely linked to receiving a loan. Of course, the borrowers consider this fund as an asset. Besides his contribution to the grand/compulsory account, each member also has to save an amount every month. This account is called basic savings. All institutions ask the same amount from their clients to add to these savings. When the loan is repaid, the member can withdraw the grand and basic savings, that is if he withdraws his membership from the microfinance institution. Voluntary savings are not an obligatory part of accessing credit services; voluntary savings services are provided to members, so that they can deposit or withdraw according to their needs.

The grand and basic savings are useful for the members, but also for the microfinance institution. They serve as an additional guarantee mechanism to ensure loan repayment, help to build up the asset base of the clients, provide funds for emergencies, and provide information to the staff of the institutions on the ability of the members to deal with cash flow and periodic payments (screening). The microfinance institutions are obligated by national government rule to separate the savings into these accounts.

Finally, when looking at the balance sheet of the microfinance institutions there is a fourth striking account, called special savings. These are contributions by non-members or by the staff of LPKM. The interest these socially minded receive on this account is, obviously low in comparison with other alternatives. Rismansyah and Rachmanto, employees at LPKM, monthly give Rp. 5,000 of fixed savings to Bina Mitra Warga Bandung and to Kopmaba.

Legal restrictions limit the payment of interest, of a positive nominal return. If the microfinance institutions want to offer a positive nominal return, the legal form has to change; they are then regarded as a bank. One of the striking differences compared to other microfinance institutions is that the clients do not receive interest on their savings, instead the members of an institution can obtain part of the profit, i.e. dividend. In this context it is worthwhile to notice that the regulation of micro credit nowadays is under the department of co-operation and small and medium enterprises. LPKM, together with 37 other organisations in Bandung, take the initiative to try to achieve that the regulations concerning micro credit will resign under the auspices of the Central Bank. This makes it possible to develop the micro credit programmes further.

Thus the natural question arises, why do members save at the institution? The general rule is that a client can borrow up to three times his accumulated savings; so the more savings, the more a client can borrow. This rule induces members to save at the institution in order to become eligible for a loan. Members do not earn interest, as mentioned before, but they can obtain dividend. The division of dividend, if there is any profit in the past year, depends among other things on the amount of savings of a member. This can be regarded as a substitute for interest.

In table 7.2 the profit distribution as used by the institution Kopmaba is reproduced. The same profit distribution is used at the other microfinance institutions, but with minor differences. Kopmaba distributes 45 per cent of the profit among its members: dividend to the best savers, and a percentage to the best borrowers (Balal Jasa Pinjaman). Every member receives shares depending on the amount they save or borrow. When a member saves for instances Rp. 1,000, he receives one share, and the profit is distributed to the members according to the number of shares they own. This mechanism is a good incentive to members to save at the institution, but unfortunately most institutions do not make a profit. The same method is used for borrowers but there is an extra condition: that the borrower must repay the instalment every time, and if the borrower misses just one repayment he receives no profit. The other ledgers are shown in table 7.2.

Table 7.2 Profit distribution microfinance institution Kopmaba

Percentage	Distribution
22.5%	Dividend (distributed among best savers)
22.5%	Balas Jasa Pinjaman (BJP; distributed among best borrowers)[13]
25%	Retained earnings
10%	Reserved for management (used for advice by management)
5%	Social welfare
5%	Staff welfare (like a bonus)
5%	Education
5%	Development working area

Source: LPKM

The basic and grand savings act as a form of collateral, since generally they are not available for withdrawal when a loan is outstanding. By being required to set aside funds as savings, borrowers cannot utilise those funds for their business activities or other investments. Because the members of the institutions do not earn interest, this results in an opportunity cost that is equal to the difference between what they earn now (i.e. zero per cent) and the return they could have earned.

[13] Government regulation: minimum distribution of dividend and BJP must be 30 per cent.

§ 7.2.1 Future

One of the goals of LPKM is to transform the microfinance institutions into small (formal) banks, including the ability to mobilise savings. This makes sense for several reasons. First, savings provide a relatively inexpensive source of capital for relending. Second, the depositors of today can be tomorrow's borrowers, so this creates a client pool. Third, building savings can increase the welfare of the members, which is the objective of the microfinance industry, by building assets that can act as collateral. They can use this asset for example to reduce the volatility in consumption.

Just as there are principles for lending to the poor, there are principles for providing savings services that the several microfinance institutions need to be aware of. To attract deposits from members the following principles need to be adhered to. The desired savings instruments must offer safety, convenience, ready access to money, and a positive return.

Regarding safety we would like to make the following remarks. Regarding the collecting of savings, it is the customer who must trust the microfinance institution. Deposit clients must be convinced that the microfinance institution staff is competent and honest. The information we acquired from the staff of LPKM and through surveys and conversations with the members points out that members are convinced that their savings are safe. The saver knows the staff of the microfinance institutions: they meet at trainings, meetings and when they apply for a loan. Another reason they trust the microfinance institutions is that most institutions work near the office of the institute. People in the community are familiar with each other usually well before a microfinance institution has started. All microfinance institutions provide bankbooks, which specifies the amount of savings and the date it was deposited. To cover the cost, the microfinance institutions charge an entrance fee. Caution is essential, since the Indonesian people have a tendency to associate additional charges with corruption. Ultimately, however, word of mouth is the best form to ensure trust. One man living in an area of Cibaduyut, a tight community with an informal leader, said that he was very hopeful about the founding of a new microfinance institution. If the institution does something good, other people in the area will know it very quickly. If the institution does something bad, they will talk about that for years to come.

A bank must be financially sustainable if it wants to provide services on a widespread and continued basis. To accomplish this transformation, certain key features of the microfinance institutions that are members of LPKM need to be changed. Until now, none of the microfinance institutions are financially sustainable. Financial self-sufficiency is essential for making financial services widely available to micro-enterprises, they can expand to meet the demand of their customers and thus help the poor. To this end, the microfinance institutions can rely more on the savings of their members as a relatively cheap source of capital. This does necessarily mean that they have to pay interest on their savings, because several studies show that savers value liquidity over returns and a well-suited design of the savings instruments (Charitonenko, Patten and Yaron, 1998). However, research may be suitable to look at whether the increase in savings (reduction in capital costs) outweighs the extra interest costs. As mentioned above, savers value ready access to their money, i.e. liquidity. This is where a problem arises for the microfinance institutions, because they have at this moment low liquidity. This can even undermine the stability of a healthy financial institution.

§ 7.3 Subsidies

LPKM needs to keep an eye on the efficiency of the microfinance institutions, but it must also mind its own efficiency. The staff at LPKM receives a fixed salary from the university, and the funds from donors are fully redistributed to the microfinance institutions, so no money is ever retained for the purposes of LPKM or the Parahyangan Catholic University. Especially in the light of the expansion of member institutions (during our research period eight new institutions became affiliated with LPKM), it is important to work efficiently since the time and the money available for giving training, approving of loan proposals and checking financial reports is limited. Money from donors can be very unstable and can threaten the existence of a microfinance institution. Therefore, microfinance institutions want to be financially independent, but interviews with the staff of LPKM suggest that this is not a concern. LPKM expects sources to be available in the near future. For detailed information on the subsidies, see Appendix C.

LPKM has to make sure that the donation of the money or the granting of concessional loans does not dilute its social mission and change their philosophy. Until now donors only want to see a monthly financial report. The involvement of donors and the local government in providing microfinance has its pros and cons. Semi-government microfinance programmes are sometimes perceived as social welfare instead of economic development efforts, which results in problematic and depressing repayment rates. They can be a source of learning, since many donors have worked with specific institutions in specific regions and with certain approaches. Sharing these experiences can benefit donors as well as LPKM. Personally, we think this is not a (potential) problem for LPKM, but nevertheless we would like to warn LPKM to be cautious about this issue.

§ 7.4 Repayment

Nowadays, microfinance institutions are forced to operate on a full-cost recovery basis. A common explanation being is that micro-credit programmes that can cover their own cost can expand and serve more clients. The purpose of the microfinance institutions is to provide the poor with long-term continued access to financial services. This can only be achieved if all costs are covered. If an institution is inefficient in delivering credit and consequently needs to raise its interest rate, clients may not find value in the credit offered and the institutions will have difficulties to stay in business.

The next subsections outline the financial data to study the performance in another context and to increase the understanding of the programme. The financial performance indicates whether the programme is well designed: are the mechanisms used effectively?

§ 7.4.1 Repayment microfinance institutions

Although a detailed analysis of the financial performance and health of the microfinance programmes belonging to LPKM was neither carried out nor our focus, a first glance reveals that they are not financially sustainable. This conclusion is reached after looking at the financial reports and from interviews with the staff of LPKM.

Ideally, we would like to analyse the repayment performance of the individual microfinance institutions, but due to a combination of language difficulties, missing or incorrect financial reports, and time pressure, this was impossible. Therefore, we have chosen to infer the success of the microfinance institutions by looking at the repayment of loans granted by LPKM. This certainly has drawbacks[14], but it will provide an insight into how the mechanisms used and the design of the programme provides incentives to the microfinance institutions and the clients to pay back the loans.

LPKM forces the microfinance institutions to attain and retain better performance and at the same time provide incentives to adopt the lending techniques that have proven to be valuable.
While social capital is important in group lending contracts, LPKM utilises this capital to improve the repayment rates of the individual liability microfinance institutions. The financial and social meetings elicit several types of group dynamics, which may increase repayment rates. Another reason why this technique can be helpful, is that the financial resources are scarce, so when another micro credit institution is running its business unsuccessfully, this means that there is less money to redistribute by LPKM.

Generally, high repayment rates help LPKM and the microfinance institutions to meet the demand of their target group. However, high repayment rates do not mean that there is more money to redistribute if the costs are not contained. Moreover, it does not automatically mean that the programme will have a social impact.

The microfinance institutions are forced by LPKM to be financially self-sufficient, so that more members and institutions can be served. The loan recovery rates are significantly influenced by the interest rate charged to the members, the repayment of the borrowers and the operational efficiency of the microfinance institutions, which will not be explicitly addressed though this does not suggests it is insignificant. Table 7.3 shows the repayment performance of the microfinance institutions. Appendix D, shows how this is calculated. The outcomes of these calculations indicate how effectively the programmes established the basic microfinance (proven) principles, even though these repayment performance are blurred by various biases (Murdoch, 1999).

[14] Some microfinance institutions receive loans from moneylenders other than LPKM, so it is possible they use these loans to pay off the loans at LPKM. To measure the success in terms of lack of delinquency can be totally inappropriate to judge the successful achievement of the social mission of the microfinance institutions. To illustrate this we use an exaggerated example: an institution can use savings and perhaps other financial sources to show a respectable performance record, but until now has not made any loans to their members. One must bear in mind that the financial performance may be blurred by other events and influenced by many issues (e.g. circumstances beyond one's control, like financial crisis and natural disaster). While the mechanisms used are efficient and effective in this specific surroundings.

Table 7.3 Repayment performance from May 2000 until April 2001

Microfinance institution	**May/June/July**	**Aug/Sept/Oct**	**Nov/Dec/Jan**	**Feb/March/April**
BMW Bandung	100%	100%	95%	62%
Kopmaba	67%	24%	25%	30%
Anugerah	N A	N A	N A	N A
Mitra Sejahtera	100%	100%	100%	100%
Mitra Umat	N A	N A	N A	N A
Mitra Mandiri	0%	100%	100%	100%
Mitra Wargi Saluyu	N A	N A	N A	N A
Surya Mandiri	N A	N A	N A	N A
Dulang Perak	N A	N A	N A	N A
Multi Usaha	79%	42%	17%	0%
Setia Kawan	N A	N A	N A	N A
Tatali Wargi	100%	84%	69%	100%
Mega Prima	100%	67%	100%	100%
Paguyuban Warga	N A	N A	N A	N A
Koprima	N A	N A	N A	N A
Cibangkong Sebelas	100%	100%	100%	100%
BMW Sumadang	100%	61%	15%	0%
Batulonceng	N A	N A	N A	N A
Nurul Amal	50%	25%	0%	0%
Kowardes Berkah	100%	100%	100%	59%
Baruna Siribon	N A	N A	N A	N A

Source: LPKM

Preferably, we would like to compare the repayment rate over a longer period of time- to see whether financial performance is improving or deteriorating. A longer period of time also contributes to the reliability. Unfortunately, this was not possible due to the absence of relevant data, which forced us to adjust our initial intention. The rates are calculated over a short period of time, one year, but nevertheless they give an insight into the above mentioned relation, the relative financial performance of the institutions, and an early assessment of the newly founded institutions.

§ 7.4.2 Repayment members of microfinance institutions

As mentioned before, it was not possibly to make a financial analysis of the repayment performance of the individual microfinance institutions. However, the member respondents gave us a clear insight into the repayment performance, which will be presented here. First, we look at the late repayments of the borrowers. As table 7.4 shows, 72 per cent of the respondents made a late repayment in the past. This indicates a poor repayment and can lead to financial difficulties at the institutions. With individual loans there is only individual liability, so the single borrower carries the burden. For microfinance institutions this makes it harder to enforce the loan. The main reason members could not repay the instalment on time, was because of business failure (37 per cent), especially due to little sales. The second reason was illness of the borrower, which meant he did not have an income. Other reasons for late repayments were natural disasters, emergencies or borrowers that had to pay other debts first.

Table 7.4 Late repayment (Respondents: 63 members)

(1) Did you have at least one late repayment in the past?	**(%)**
Yes	72
No	28
(2) What were the reasons for the late repayment?	**(%)**
Business failure	37
Illness of borrower	31
Not clear	8
Had to buy every day articles et cetera	6
Natural disaster	4
Other	14
(3) How difficult was it for you to make repayments in the past month?	**(%)**
Very difficult	18
A little difficult	58
Not difficult	23
(4) What sources did you use for your loan repayment in the past month?	**(%)**
Income from self-employment	35
Income from a wage	25
Sell agriculture and livestock products	19
Sell durable goods of production material	8
Borrow money from family (informal)	6
Other	7
(5) If you have difficulties to repay, what did you try to make the repayment?	**(%)**
Borrow from family or friends	42
Savings	31
Borrow from individual member	7
Went to institution and asked about rescheduling	7
Borrowed from the group	4
Tried to get other funds	4
Other	6
(6) When you had difficulty paying the instalment, which expenditures did you reduce?	**(%)**
Daily	48
Clothing	42
Food	6
Fertiliser and pesticide	3
(7) During the most difficult month, did family members work more?	**(%)**
Yes	80
No	20

However, the high percentage of members with a late repayment in the past does not tell us much about the current situation. When we look at the repayments of the last month, 18 per cent of the respondents found it very difficult to pay the instalment. For a larger percentage it was not difficult to make last month's repayment. The three main sources used for the repayment in the last month are income from self-employment, income from wage and selling agricultural and livestock products.

When a member has no money to repay the instalment and has an individual loan, 42 per cent of the respondents borrows money from family or friends and 31 per cent uses their savings to repay. A problem that often arises when members cannot repay their loan is that they ask for another loan somewhere else to pay off the old one (loan recycling). But according to the respondents, they do not borrow from commercial banks or informal moneylenders to pay off their loan. If a member has no other source he can use to repay, he often goes to the microfinance institution and asks about rescheduling the loan term. Not only does the delinquent borrower try to use other funds to repay, by reducing expenditures he tries to save money to repay the loan. When there are difficulties with repayment the main expenditures reduced are the daily ones (48 per cent) and clothing (42 per cent). Besides saving money by reducing expenditures, 80 per cent answered that family members worked more in order to repay the loan.

Usually the members take the instalment to the institution. At some institutions one member of staff is responsible for collecting the instalments. This is done daily, weekly or monthly, depending on the individual loan agreement. This shows a willingness to adapt to local circumstances. The largest groups, who repay the instalments daily, are the small-scale enterprises and the becak drivers. Factory labourers and borrowers with a weekly income usually make weekly repayments. Civil servants and pensioners repay monthly. However, when a member does not bring the instalment to the institution on time in most cases the staff visits (see table 7.4) the member to discuss the problem and ask for the reason. They discuss how to develop the small-scale business of the member, and sometimes the staff makes a new loan agreement or reschedules the loan. According to the staff, it happens often that the borrower says he cannot repay the instalment but it happens regularly that they are simply not willing to repay. Therefore, the staff not only visits the member but also asks neighbours, other members or relatives whether the delinquent borrower really has no money and whether his business is really going badly.

§ 7.5 Rescheduling

It is obvious that due to the financial crisis many microfinance institutions ran into difficulties. Because of the sharp increase in non-performing loans of members at the start of the crisis and afterwards, the microfinance institutions failed to meet their obligation. LPKM responded adequately to these growing difficulties by rescheduling the loans of the microfinance institutions with the most severe problems. Also the microfinance institutions felt that something had to be done and that rescheduling was one of the possibilities to solve these issues. Thus, they provided liquidity (breathing space) and prevented the microfinance institutions from taking hard measures. Rescheduling a loan means extending the loan term or changing the payment schedule or both. When a microfinance institution is unable to repay a loan due to illness, natural disaster, mismanagement or crisis, it can also be possible to refinance the loan. Refinancing is generally more risky than rescheduling, and the assistor has to have financial resources for this health care support. In August of 1998LPKM decided to reschedule the loans of three microfinance institutions (Kopmaba, Bina Mitra Warga Bandung, and Bina Mitra Warga Sumedang).

LPKM rescheduled the loans after the financial crisis as follows. The staff of LPKM first looked at the principal amount that was outstanding; next, the interest was calculated which the microfinance institution would have to pay if everything went according to plan. Then, these two amounts were added up together. Subsequently, the microfinance institution and LPKM would negotiate on the term and the amount that would be transferred monthly. This whole process would lead to a longer loan term without additional interest cost for the microfinance institutions. LPKM might consider levying an additional fee to make up for lost revenue on the loan due to the rescheduling, it is outstanding for a longer period and, therefore, should generate more revenue. Rachmanto, an employer at LPKM, said the reason that they do not charge additional interest is because this will have an adverse effect on the financial stability of the microfinance institutions. Charging extra interest would disturb and deteriorate the balance sheet of vulnerable financial institutions.

Chapter 8 Concluding remarks

This paper has tried to make a contribution to the literature on microfinance by providing an elaborate description and analysis of a relatively new microfinance programme. By examining the microfinance programme at the Parahyangan Catholic University Centre for Community Services, we tried to link adverse selection, moral hazard, auditing and enforcement problems, caused by asymmetric information, to the practice of microfinance. By scrutinising the theories concerning microfinance practices and empirical studies striking deviations were unveiled. In the process of achieving this goal we presented a thorough description of the microfinance programme initiated by LPKM. This once more emphasises that theory and practice can differ, and that the programme is unique allthough there are similarities with other microfinance programmes.

First, we addressed the problems caused by asymmetric information. LPKM deals with this by making use of group lending contracts. While other microfinance programmes exploit group benefits for initial loans and small loan amounts, the institutions affiliated with LPKM use group solidarity and local information for loan amounts exceeding Rp. 15,000,000. Until now the group lending contracts are not impeccable, the appropriate design has still too be drafted. What is also rather striking is that they make emphatical use of meetings to obtain and distribute information in order to cope with moral hazard and adverse selection. To enforce repayment, LPKM and the microfinance institutions apply progressive lending and dynamic incentives. These mechanisms function reasonably well, but it is hard to judge how consistent LPKM executes its rules, since it is a relatively new programme and because of the financial crisis in 1998. The incentives that stem from these mechanisms depend heavily on how strictly the rules are enforced. LPKM must not be shallow to apply their rules. Badly performing institutions do not receive additional loans, but it is not unlikely that they will receive loans again in the future.

Furthermore, we linked the literature on outreach and financial issues related to sustainability to this programme. While many other microfinance institutions aim at serving women for several reasons, the institutions affiliated with LPKM do not have a specific focus on women. Our research shows that LPKM does not reach the poorest segment of the community. LPKM and the microfinance institutions realise that they do not reach the poorest of poor, but try to develop the community and with it the local economy to alleviate mainly urban poverty. To meet the demand of their target group and to ease the process of lending to the less fortunate, more than financial services is provided. The fact that microfinance institutions make use of savings as a substantial source of funding indicates that the clients are indeed not the poorest people of Indonesia. The funding of LPKM depends on subsidies from all kind of sources, like an NGO in Canada, UNPAR, and the local government. LPKM and the microfinance institutions are therefore not financially sustainable. These providers of subsidies do not interfere with the activities and policy of LPKM but only demand a monthly financial report.

The financial crisis of 1998 had a significant impact on the repayment performance of microfinance institutions and their members. The members could not repay their loans, and therefore many loans to the microfinance institutions had to be rescheduled to prevent bankruptcy. The current situation of repayment by the affiliated microfinance institutions shows much diversity: while some have little difficulties to repay, others could not meet their financial obligations in the last few months. Due to this diversity LPKM started to strengthen the cohesion between the institutions, which resulted for example in a merger between two microfinance institutions. To ensure high repayment now and in the future LPKM makes extensive use of social intermediation. Social intermediation can best be understood as the process of building human and social capital required for sustainable financial intermediation with the poor. In addition, providing training such as entrepreneurship skills and social services such as health care, builds the human and social capital and can improve the ability of the poor to operate for instance their own small-scale enterprises. For LPKM the social intermediation is very important, because by building the human and social capital they hope the Indonesian people will learn to trust each other again.

Appendix A Questionnaire form Members of Microfinance Institution

Pertanyaan untuk anggota Lembaga Keuangan Mikro/Koperasi
Questions for members of the Microfinance Institution

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1. Nama anda? *(What is your name?)*
   ……………………………………………………………………………………

2. Jenis Kelamin? *(What is your gender?)*
   - ❑ Perempuan. *(Female)*
   - ❑ Laki-laki. *(Male)*

3. Pekerjaan? *(What is your occupation?)*
   ……………………………………………………………………………………

4. Apakah anda sudah menikah? *(Are you married?)*
   - ❑ Ya. *(Yes*)
   - ❑ Tidak. *(No)*

5. Jumlah anak? (*How many children do you have?)*
   …………………………………………………………………………………….

6. Bagaimana cara anda mencari informasi tentang lembaga keuangan micro/koperasi berserta programnya? *(How did you find out about the microfinance institute and the programme?)*
   ………………………………………………………………………………………………………
   ………………………………………………………………………………………………………
   ………………………………………………………………………………………………………
   ……………………………………

7. Mengapa anda menjadi anggota lembaga keuangan micro/koperasi? *(Why did you apply to the microfinance institute?)*
   - ❑ Karena training yang diberikan oleh Lembaga Keuangan Micro/Koperasi? *(For the training given by the microfinance institute.)*
   - ❑ Karena kebutuhan untuk meminjam. *(I needed the loan.)*
   - ❑ Karena bunga/jasa yang kecil. *(Because of the low interest.)*
   - ❑ Karena tidak mendapatkan pinjaman dari tempat lain (dari Bank). (*I cannot get a loan elsewhere (formal bank)*

- ❑ Lain-lain (sebutkan), ………………………………….. (*Other*)

8. Apa tujuan anda mengajukan permohonan pinjaman/kredit? **(***What was the original purpose of the loan you applied for?)*
   - ❑ Untuk menjalankan usaha yang ada. (*Money to run the existing business.)*
   - ❑ Untuk memperluas usaha. (*Money was needed to expand the existing business.)*
   - ❑ Untuk memulai usaha baru. (*Money was needed to start a business for the first time.)*
   - ❑ Untuk biaya pengobatan. *(Medical expenses.)*
   - ❑ Untuk keperluan keluarga. *(Expenditure related to family.)*
   - ❑ Untuk upacara sosial (Sunatan, Perkawinan dll). *(Social ceremonies.)*
   - ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

9. Sebelumnya atau apakah anda pernah mendapatkan pinjaman bersama (kelompok) dengan anggota lainnya? *(In the past did you or do you get a loan together with other members?)*
   - ❑ Ya. *(Yes)*
   - ❑ Tidak, silahkan lanjutkan dengan pertanyaan nomor 23 (*No, continue at question number 23)*

10. Bila Ya, apakah anggota kelompok yang mendapat pinjaman tersebut adalah? *(If yes, the people in your group are……..?)*
    - ❑ Tergantung/relatif. *(Relatives)*
    - ❑ Teman. *(Friends)*
    - ❑ Orang lain (tidak kenal). *(Strangers)*
    - ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

11. Berapa jumlah anggota dalam satu kelompok (tanggung renteng)? *(How many member are there in your group?)*
    - ❑ Dua orang. *(2 people)*
    - ❑ Tiga orang. *(3 people)*
    - ❑ Empat orang. *(4 people)*
    - ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

12. Apakah anda dapat memilih, siapa yang anggota dalam satu kelompok? (*Could you choose the people with whom you formed a group?)*
    - ❑ Ya. *(Yes)*
    - ❑ Tidak. *(No)*

13. Bila anda membentuk kelompok, mengapa anggota tersebut yang anda pilih? *(If you could form a group on your own, why did you chose these people?)*

- ❑ Reputasinya baik. *(They have a good reputation)*
- ❑ Sudah kenal cukup lama. *(We get along well)*
- ❑ Tetangga. *(We are neighbours)*
- ❑ Tidak tahu. *(Do not know)*
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

14. Apakah ada jadwal pertemuan (tetap) bersama kelompok? *(Does your group meet regularly?)*
    - ❑ Ya. *(Yes)*
    - ❑ Tidak. *(No)*

15. Apakah kelompok anda mempunyai peraturan? *(Did your group make any rules?)*
    - ❑ Ya. *(Yes)*
    - ❑ Tidak. *(No)*

16. Bila ya, bagaimana peraturannya? *(If yes, what kind of rules?)*
    ……………………………………………………………………………………………………
    ……………………………………………………………………………………………………
    …………………………………………………

17. Apakah kelompok anda mempunyai tabungan? *(Does your group have a savings scheme?)*
    - ❑ Ya. *(Yes)*
    - ❑ Tidak. *(No)*

18. Apakah ada anggota kelompok anda yang mempunyai masalah dalam membayar cicilan? *(Where there any members in your group who had problems repaying their instalment?)*
    - ❑ Ya. *(Yes)*
    - ❑ Tidak. *(No)*

19. Bila ya, siapa yang membantu? *(If yes, did they receive help from anybody?)*
    - ❑ Saya sendiri. *(From myself)*
    - ❑ Anggota kelompok yang lain. *(From somebody else from the group)*
    - ❑ Kelompok secara ber sama-sama. *(From the group as a whole)*
    - ❑ Lain-lain (sebutkan), …………………………….. (*Other*)

20. Bantuan apa yang diberikan pada anggota kelompok tadi? *(What kind of help was offered to this person?)*
    - ❑ Bantuan keuangan. *(Financial support)*
    - ❑ Lain-lain (sebutkan),……………………….. (*Other*)

21. Sangsi apa yang digunakan kelompok untuk menghindarkan masalah tadi di kemudian hari? (*What kinds of sanctions were used by the group to avoid problems in the future?)*

……
……
…………………………………………

22. Siapa yang menegur anggota kelompok yang tidak dapat membayar cicilan? *(Who addressed the person of the group when he could not pay the instalment?)*
    - ❑ Saya sendiri. *(I did)*
    - ❑ Anggota kelompok lain. *(Somebody else from the group did)*
    - ❑ Kelompok secara bersama. *(The group as a whole did)*
    - ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

23. Sampai sejauhmanakah anda mengenal anggota lain dari lembaga keuangan micro/koperasi? *(How well do you know the other members from the microfinance institution?)*
    - ❑ Sangat baik *(Very well)*
    - ❑ Baik. (*Good*)
    - ❑ Kurang baik. *(Not good)*
    - ❑ Tidak mengenal. *(Hardly)*

24. Apa saja yang suka dibicarakan dalam pertemuan/rapat? *(What is discussed at the meetings?)*
    - ❑ Laporan keuangan. *(Financial report)*
    - ❑ Peraturan-peraturan Lembaga Keuangan/Koperasi. *(Regulations)*
    - ❑ Keterlambatan pembayaran angsuran. *(People who are too late with their payment)*
    - ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

25. Berapa nilai bunga/jasa perbulan tertinggi yang akan anda bayar? *(What is the highest monthly interest rate you are willing to pay?)*
    ……
    ……………………………………………………………………………………..
    ……………………………………………………………………

26. Berapa nilai bunga/jasa perbulan tertinggi yang dapat anda bayar? *(What is the highest monthly interest rate you are able to pay?)*
    ……
    ……
    …………………………………………………

27. Berapa nilai bunga/jasa yang biasa anda bayar? *(How much interest are you paying on your current loan?)*
    ……
    ……
    …………………………………………………

28. Berapa jumlah pinjaman yang pernah anda terima? *(What amount did you receive as a loan?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………

29. Apakah anda suka membayar lebih jasa/bunga untuk jumlah pinjaman yang besar? *(Would you be willing to pay more interest in exchange for a higher loan?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

30. Apakah anda mendapatkan pinjaman selain dari lembaga keuangan mikro/kopearsi? *(Do you have outstanding loans anywhere else than at your microfinance institution?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

31. Bila anda mendapatkan pinjaman selain dari lembaga keuangan mikro/koperasi, dari mana sumber pinjaman tersebut? *(If you have loans outstanding somewhere else, what is the source of these other loans?)*
- ❑ Keluarga. *(Family*)
- ❑ Bank. *(Formal bank)*
- ❑ Modal Ventura. *(Venture capitalist)*
- ❑ Sumber informal. *(Informal agent*)
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

32. Bilamana di tempat anda tidak ada lembaga keuangan mikro/koperasi, apakah anda tetap akan menjalankan program lembaga keuangan mikro/koperasi? *(If there was no microfinance programme, would you still undertake the project?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

33. Bilamana anda tetap menjalankan lembaga keuangan mikro/koperasi, apakah dalam lingkup kerja/program yang sama? *(If you were to undertake the project anyway, would the scale be the same?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

34. Bilamana Ya, dari manakah anda mendapatkan dana bantuan? *(If yes, where would you get the funds from?)*
- ❑ Tabungan. *(Savings)*
- ❑ Menjual kekayaan. *(Sell property)*
- ❑ Meminjam dari sumber informal. *(Borrow from informal sources)*

- ❑ Meminjam dari Bank. *(Borrow from formal bank)*
- ❑ Menjual barang dan meminjam. *(Both sell product and borrow)*
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

35. Berapa jarak antara rumah anda dengan Lembaga Keuangan Mikro/koperasi? (*What is the distance from your home to the microfinance institution, in kilometres?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
……………………………………………………

36. Apakah anda akan datang bilamana ada pelatihan yang diberikan oleh lembaga keuangan mikro/koperasi? *(Do you go to the training provided by the microfinance institution?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

37. Kapan pelatihan tersebut diberikan oleh lembaga keuangan mikro/koperasi dan berapa lama waktu yang dibutuhkan untuk sebuah pelatihan, dalam hitungan menit? *(When there is a training given by the microfinance institution, how long does the training normally takes, in minutes?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
……………………………………………………

38. Bagaimana menurut anda berkaitan dengan ketepatan waktu pertemuan/rapat, dalam hitungan menit? *(What do you feel is the appropriate duration of a meeting, in minutes?)*
…………………………………………………………………………………………………
……………………………………………………

39. Apakah anda pernah mengalami keterlambatan membayar angsuran, minimal satu kali keterlambatan? *(Did you have at least one late repayment in the past?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

40. Bila ya, apakah alasan yang anda berikan berkaitan dengan keterlambatan pembayaran tersebut? *(If yes, what were the reasons for the late repayment?)*
- ❑ Bencana alam. *(Natural disaster)*
- ❑ Kegagalan usaha. *(Business failure)*
- ❑ Sakit. *(Own illness)*
- ❑ Kematian anggota keluarga. *(Death of family member)*
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

41. Apakah pengurus lembaga keuangan/koperasi akan datang ke rumah and/a bilamana anda tidak dapat membayar angsuran tepat waktu? *(Did the staff of the institution come to you when you*

could not repay the instalment?)

- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

42. Bilamana anda terlambat membayar angsuran, apa yang lembaga keuangan/koperasi lakukan terhadap anda? *(If you had a late payment, what did the microfinance institute do when you could not repay the instalment on time?)*

- ❑ Membuat perjanjian pinjaman baru. *(Made a new loan agreement)*
- ❑ Tidak mendapatkan pijaman dimasa yang akan datang. *(Banned me for further loans)*
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

43. Bilamana anda mendapatkan kesulitan membayar angsuran tepat waktu, usaha apa yang anda lakukan untuk mengatasi persoalan tersebut. *(If you have trouble paying the instalment on time, what source do you use to make the repayment?)*

- ❑ Tabungan. *(Savings)*
- ❑ Meminjam dari kaluarga atau kawan. *(Borrowed from family or friends)*
- ❑ Menjual kekayaan. *(Sold property)*
- ❑ Meminjam dari kelompok. *(Borrowed from the group)*
- ❑ Meminjam dari anggota kelompok. *(Borrowed from individual member)*
- ❑ Meminjam dari rentenir. *(Borrowed from informal money lender)*
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

44. Sejauhmana kesulitan yang anda rasakan untuk membayar angsuran pada akhir bulan. *(How difficult was it for you to make repayments in the past month)*

- ❑ Sangat sulit. *(Very difficult)*
- ❑ Sedikit. *(A little difficult)*
- ❑ Tidak sulit. *(Not difficult)*

45. Pada saat anda mendapatkan kesulitan untuk membayar angsuran, maka jenis biaya hidup apa yang anda kurangi? *(In the past when you had difficulty paying the instalment, what kind of expenditures did you reduce?)*

- ❑ Biaya makanan. *(Food)*
- ❑ Biaya kebutuhan harian. *(Daily)*
- ❑ Biaya pakaian. *(Clothing)*
- ❑ Biaya pupuk dan pestisida. *(Fertilizer and pesticide)*
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

46. Selama anda dalam bulan yang sulit, apakah anggota keluarga bekerja lebih? *(During the most difficult month, did family members work more?)*

- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

47. Jenis usaha apa yang anda gunakan untuk membayar angsuran pinjaman? *(What sources did you use for your loan repayment in the past month?)*
- ❑ Menjual hasil pertanian dan produk kebutuhan hidup. *(Sold agriculture and livestock products)*
- ❑ Menjual barang. *(Sold durable goods of production material)*
- ❑ Gaji. *(Wage income)*
- ❑ Penghasilan pribadi. *(Income from self-employment income)*
- ❑ Tunai. *(Cash in hand)*
- ❑ Meminjam dari saudara/keluarga atau sumber informal lainnya. *(Borrowed from family (informal))*
- ❑ Meminjam dari lembaga formal. *(Borrowed elsewhere (formal))*
- ❑ Lain-lain (sebutkan), ………………………………..(*Other*)

48. Bilamana anda dapat membayar angsuran tepat waktu, apakah menurut anda, anda akan mendapatkan pinjaman kembali? *(If you pay all instalments on time do you think you can get another loan?)*
- ❑ Ya. Tentu. *(Yes, definitely)*
- ❑ Mungkin Ya. *(Probably)*
- ❑ Mungkin Tidak. *(Probably not)*
- ❑ Tidak tahu. *(Do not know)*

49. Bilamana anda selesai membayar keseluruhan pinjaman, apakah anda ingin mengajukan pinjaman kembali? *(If you have already successfully repaid a loan, did you get another loan?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

50. Pernahkan anda mengajukan pinjaman, tetapi anda tidak mendaptkannya? *(Has it ever happened in the past that you applied for a loan but did not get?)*
- ❑ Ya. *(Yes)*
- ❑ Tidak. *(No)*

51. Bila anda pernah mendapatkan pinjaman, apa alasan/dasar anda mengajukan pinjaman? *(If you never refused a loan in the past, what was the reason?)*
…………………………………………………………………………………………………
……………………………………………………………

52. Jenis tenggang waktu pinjaman yang anda sukai? *(What is the loan duration you prefer?)*
- ❑ Kurang dari atau sama dengan 3 bulan. *(Less than 3 months)*
- ❑ Antara 4 dan 6 bulan. *(4-6 months)*
- ❑ Antara 7 dan 12 bulan. *(7-12 months)*
- ❑ Antara 13 dan 24 bulan. *(13-24 months)*
- ❑ Lebih dari 25 bulan. *(More than 25 months)*

53. Jenis pembayaran angsuran? *(Preferred repayment frequency*)

- ❑ Mingguan *(1 week)*
- ❑ Dua Mingguan *(2 weeks*)
- ❑ Tiga Mingguan *(3 weeks)*
- ❑ Bulanan *(1 month)*
- ❑ Antara 1 dan 6 bulan. *(Between 1 and 6 months*)
- ❑ Lebih dari 6 bulan. *(More than 6 months)*

54. Jenis pertolongan/bantuan/pendampingan apa yang anda harapkan dari lembaga keuangan micro/koperasi selain pemberian pinjaman? *(What kind of help do you receive from the institutions, besides loans?)*

- ❑ Pelatihan pembukuan. *(Training book keeping skills)*
- ❑ Pelatihan manajemen/organisasi. *(Training management organizational skills)*
- ❑ Pelatihan Kewirausahaan. *(Entrepreneurship)*
- ❑ Keseluruhan yang disebutkan di atas. *(All of the above)*
- ❑ Lain-lain (sebutkan), …………………………………..(*Other*)

55. Apakah anda berharap menerima pertolongan/bantuan/pendampingan tambahan dari lembaga keuangan mikro/koperasi? (*Do you wish to receive more help from the institution?)*

- ❑ Tidak. *(No)*
- ❑ Ya. *(Yes)*

56. Bila Ya, jenis pertolongan/bantuan/pendapingan tambahan apa yang anda harapkan? *(If yes, what other kind of help would you like to receive from the institution?)*

…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………………

TERIMA KASIH ATAS KERJASAMANYA

(THANK YOU FOR YOUR COOPERATION)

Appendix B Questionnaire form Staff Members of Microfinance institution

PERTANYAAN UNTUK STAFF LEMBAGA KEUANGAN/KOPERASI
(QUESTIONNAIRE FOR STAFF OF MICROFINANCE INSTITUTIONS)

1. Apa nama Lembaga Keuangan/Koperasi anda? (*What is the name of your institution?)* ……………………………………………………………………………………………….
2. Apakah posisi anda dalam lembaga tersebut? *(What is your function at the institution?)……………………………………………………………………………….*
3. Kapan Lembaga Keuangan/Koperasi tersebut berdiri, sebutkan tanggal, bulan & tahun? *(When did your institute began, what date?)…………………………………….*
4. Berapa jumlah anggota Lembaga Keuangan/Koperasi pada saat ini? (*How many members does your institute have at this moment?)……………………………………*
5. Persoalan-persoalan organisasi dan persoalan-persoalan manajemen apa saja yang pernah dihadapi? (*What kind of managerial/organisational or other difficulties did you face in the past?)*
   …………………………………………………………………………………………………
   …………………………………………………………………………………………………
   …………………………………………………………………………………………………
   ……………………………………………
6. Apakah setiap anggota hadir bilamana diadakan pertemuan? (*Is every member invited to every meeting?)*
   …………………………………………………………………………………
7. Bila tidak, Mengapa? (*If no, why is not every member invited to every meeting?)*
   …………………………………………………………………………………………………
   …………………………………………………………………………………………………
   …………………………………………………………………………………………………
   ……………………………………………

8. Bagaimana hak-hak anggota didistribusikan/diinformasikan diantara anggota dan bagaimana Lembaga Keuangan/Koperasi didirikan? *(How are the voting rights distributed among members, and how are they established?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………

9. Siapa yang memutuskan topik yang akan dibicarakan dalam sebuah rapat? *(Who decides the topics of voting at meetings?)*
   - ❑ Pengurus Lembaga/Koperasi. *(Staff)*
   - ❑ Anggota Lembaga/Koperasi. *(Members)*
   - ❑ LPKM
   - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

10. Dalam pembicaraan/topik apa anggota Lembaga Keuangan/koperasi dilibatkan? *(On what topics do members vote?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………………

11. Bagaimana anggota menggunakan hak-haknya. *(How are the votes of the members used?)*
   - ❑ Rekomendasi. *(Recommendation)*
   - ❑ Obligasi. *(Obligation)*
   - ❑ Tidak digunakan. *(Not used)*
   - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

12. Bagaimana anda menganalisa/menilai anggota baru? *(How are new members analysed?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………

13. Faktor apa saja yang menjadi bahan pertimbangan bilamana anggota ingin mengajukan pinjaman? (*Which factors do you take into consideration when a new member wants to apply for a loan?)*
   - ❑ Proposal. *(Business proposal)*
   - ❑ Masukan dari anggota lainnya. *(Opinion from other members)*
   - ❑ Masukan dari tetangga. *(Opinion from neighbours)*
   - ❑ Wawasan dari anggota itu sendiri. *(My own knowledge of the new member)*
   - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

14. Pernahkah anggota mengajukan pinjaman, tetapi tidak mendapatkannya? (*Has it ever occurred that a member who applied for a loan did not get the loan?)*
    - ❑ Ya. *(Yes)*
    - ❑ Tidak. *(No)*

15. Bilamana jawaban anda Ya, maka apa alasan yang anda berikan? *(If yes, why did not the member get the loan?)*

………………………………………………………………………………………………………
……………………………………………………………

16. Apakah anda selalu memeriksa pinjaman yang diberikan telah sesuai dengan permohonan yang diajukan dalam proposal? *(Do you check whether the members use the loan according to the business proposal?)*
    - ❑ Kadang-kadang. *(Sometimes)*
    - ❑ Setiap kali. *(Always)*
    - ❑ Tidak pernah. *(Never)*

17. Berapa jarak antara rumah anda dengan LPKM UNPAR, dalam kilometer? *(What is the distance from your home to the meeting place with LPKM (UNPAR), in kilometres?)*

………
…………………………………………

18. Berapa rata-rata lamanya waktu rapat antara anda dengan LPKM UNPAR, dalam menit? *(How long does the meeting between the staff of your institution and LPKM (UNPAR) normally take, in minutes?)*

    ………………………………………………………………………………………………………
    ……………………………………………………………

19. Menurut anda, berapa lama waktu yang tepat/diperlukan untuk rapat/meeting dengan LPKM UNPAR, dalam hitungan menit? *(What do you feel is the appropriate duration of a meeting with LPKM (UNPAR), in minutes?)*

    ………………………………………………………………………………………………………
    ……………………………………………………………

20. Berapa lama waktu yang dibutuhkan bilamana ada pertemuan antara anda dengan anggota, dalam hiungan menit? *(How long does the meeting between the staff of your institution and your members normally take, in minutes?)*

    ………………………………………………………………………………………………………
    ………………………………………………………………………………………………………
    ………………………………………………………………………………………………………
    ……………………………………………

21. Menurut anda, berapa lama waktu yang tepat/diperlukan untuk rapat/meeting bersama anggota, dalam hitungan menit? *(What do you feel is the appropriate duration of a meeting with your members, in minutes?)*
…………………………………………………………………………………………………
…………………………………………………………

22. Untuk jenis pekerjaan apa angsuran pinjaman dilakukan dengan cara pembayaran angsuran harian? *(For what occupations do you collect the instalments daily?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
……………………………………………

23. Untuk jenis pekerjaan apa angsuran pinjaman dilakukan dengan cara pembayaran angsuran mingguan? *(For what occupations do you collect the instalments weekly?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
……………………………………………

24. Untuk jenis pekerjaan apa angsuran pinjaman dilakukan dengan cara pembayaran angsuran bulanan? *(For what occupations do you collect the instalments monthly?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
……………………………………………………

25. Apakah peminjam melakukan pembayaran cicilan dengan datang pada Lembaga Keuangan atau Koperasi? *(Do borrowers bring the instalment to the institution?)*
    - ❑ Ya. *(Yes)*
    - ❑ Tidak. *(No)*

26. Seberapa seringkah anda menagih untuk pembayaran angsuran pada anggota baru? *(How often do you collect the instalments for new members?)*
    - ❑ Harian. *(Daily)*
    - ❑ Mingguan. *(Weekly)*
    - ❑ Bulanan. *(Monthly)*
    - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

27. Siapa yang memutuskan seorang anggota mendapatkan pinjaman? *(Who decides whether members receive a loan?)*
    - ❑ Ketua Lembaga/Koperasi. *(The head of the institution)*
    - ❑ Seluruh staff Lembaga/Koperasi. *(The complete staff of the institution)*

- ❑ Anggota Lainnya. *(The other members)*
- ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

28. Apa saja yang menjadi alasan peminjam bilamana tidak dapat membayar angsuran pada waktu yang telah ditetapkan? *(What are the reasons borrowers say they cannot pay the instalment?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………

29. Bagaimana anda mengkonfirmasi/mengecek alasan tersebut? *(How do you check this reason?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………

30. Bilamana anda berkunjung pada para peminjam, topik apa saja yang biasanya dibicarakan? *(When you visit borrowers, what topics do you discuss?)*
…………………………………………………………………………………………………
…………………………………………………………………………………………………
…………………………………………………………………………………………………
………………………………………………

31. Berapa lama waktu yang dibutuhkan untuk pertemuan/pendampingan (kunjungan kerja) antara anda dengan peminjam, saat anda berkunjung pada anggota untuk menagih angsuran kepada anggota, dalam hitungan menit? *(How long is the meeting between borrowers and the institutions normally, when you collect the instalment, in minutes?)*
…………………………………………………………………………………………………
……………………………………………………………

32. Bilamana pembayaran angsuran tidak tepat waktu, usaha apa saja yang dilakukan untuk mengetahui penyebab keterlambatan tersebut? *(If the repayment is late, what sources do you check to find out the reason for the late payment?)*
    - ❑ Bertanya pada peminjam. *(I ask the member self)*
    - ❑ Meminta informasi pada anggota lainnya. *(I ask other members)*
    - ❑ Meminta informasi pada beberapa anggota. *(I ask relatives of the member)*
    - ❑ Meminta informasi pada tetangga peminjam . *(I ask the neighbours)*
    - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

33. Bilamana pembayaran angsuran tidak tepat waktu, apakah anda berkunjung pada anggota tersebut? *(If the repayment is late, do you visit the members?)*

- ❑ Kadang-kadang. *(Sometimes)*
- ❑ Selalu. *(Always)*
- ❑ Tidak pernah. *(Never)*
- ❑ Anggota datang ke kantor Lembaga/Koperasi. *(Members come to the institution)*

34. Apakah pernah terjadi anggota dapat membayar angsuran tetapi tidak membayar angsuran? *(Has it ever happened that members can repay, but are not willing to repay?)*
    - ❑ Tidak Pernah. *(Never)*
    - ❑ Seringkali. *(Often*).
    - ❑ Biasa terjadi. *(Regularly)*

35. Apa saja yang menjadi sumber pembayaran angsuran para anggota, dan dari manakah sumber pembayaran angsuran para peminjam? *(What are the sources of repayment; what money do the members use to repay the loans?)*
    - ❑ Menjual hasil pertanian dan kebutuhan hidup. *(They sell agriculture and livestock products)*
    - ❑ Menjual barang. *(They sell durable goods of production material)*
    - ❑ Gaji. (*Wage income)*
    - ❑ Penghasilan pribadi. *(Self-employment income)*
    - ❑ Tunai. *(Cash)*
    - ❑ Meminjam dari saudara atau teman. *(They borrow from family or friends)*
    - ❑ Meminjam di tempat lain. *(They borrow elsewhere)*
    - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

36. Apakah anggota dapat menerima pinjaman baru bila seluruh anggota membayar angsuran tepat waktu? (*Do members receive another loan when they make all the instalments on time?)*
    - ❑ Ya (pasti). *(Yes, definitely)*
    - ❑ Mungkin. *(Probably)*
    - ❑ Tidak tahu. *(Do not know)*

37. Bagaimana anda mengatasi para peminjam yang membayar angsurannya tidak tepat waktu, dan sangsi apa yang anda berikan terhadap para anggota yang terlambat membayar angsuran? (*How do you deal with borrowers who are late, what sanctions do you use for borrowers that are late with their payment?)*
    ………………………………………………………………………………………………………
    ……………………………………………………………………………………
    ………………………………………………………………………………………………………
    ………………………………………………………………

38. Jenis pembayaran apa yang lebih anda sukai, tetap atau menurun (berubah-ubah)? *(Would you prefer the timing of repayment to be regular or to vary?)*

- ❑ Tetap. *(Regular)*
- ❑ Menurun (berubah-ubah). *(Vary)*
- ❑ Tidak mempunyai pilihan. *(No preference)*

39. Berapa jam dalam satu minggu anda bekerja untuk Lembaga Keuangan/Koperasi? *(How many hours do you work at the microfinance institute, per week?)*
    - ❑ Antara 0 s/d 8 Jam. *(0-8 hours)*
    - ❑ Antara 9 s/d 16 Jam. *(9-16 hours)*
    - ❑ Antara 17 s/d 24 Jam. *(17-24 hours)*
    - ❑ Antara 25 s/d 32 Jam. *(25-32 hours)*
    - ❑ Antara 33 s/d 40 Jam. *(33-40 hours)*
    - ❑ Antara 41 s/d 48 Jam. *(41-48 hours)*
    - ❑ Lebih dari 49 Jam. *(More than 49 hours)*

40. Apakah anda menerima insentif/gaji pada saat sekarang untuk perkerjaan anda di Lembaga Keuangan/Koperasi? *(How are you rewarded for your work at the microfinance institute?)*
    - ❑ Tanpa gaji, tetapi sebagai relawan. *(No salary; voluntary)*
    - ❑ Tanpa gaji, tetapi dimasa yang akan datang saya berharap dapat menerima gaji tetap. *(No salary, but in the future I will receive a fixed salary)*
    - ❑ Tanpa gaji, tetapi dimasa yang akan datang saya berharap dapat menerima gaji berdasarkan perkembangan/kemampuan Lembaga Keuangan/ Koperasi. (*No salary, but in the future I will receive a salary based on the performance of my microfinance institute)*
    - ❑ Gaji tetap didasarkan pada perkembangan/kemampuan Lembaga Keuangan/Koperasi. *(Fixed salary plus a salary based on the performance of my microfinance institute)*
    - ❑ Gaji berdasarkan perkembangan/kemampuan dari Lembaga Keuangan/Koperasi. (*Salary based on the performance of my microfinance institute)*
    - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

41. Jenis penghargaan apa yang anda sukai untuk pekerjaan/aktivitas anda di Lembaga Keuangan/Koperasi? *(How would you like to be rewarded for your work at the microfinance institute?)*
    - ❑ Tanpa gaji, tetapi sebagai relawan. *(No salary; voluntary)*
    - ❑ Tanpa gaji, tetapi dimasa yang akan datang saya berharap dapat menerima gaji. *(No salary, but in the future I would like to receive a fixed salary)*
    - ❑ Tanpa gaji, tetapi dimasa yang akan datang saya berharap dapat menerima gaji berdasarkan perkembangan/kemampuan Lembaga Keuangan/ Koperasi. *(No salary, but in the future I would like to receive a salary based on the performance of my microfinance institute)*
    - ❑ Gaji yang jelas. *(Fixed salary)*
    - ❑ Gaji berdasarkan perkembangan/kemampuan dari Lembaga Keuangan/Koperasi. *(Salary based on the performance of my microfinance institute)*

- ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

42. Bantuan apa saja yang anda berikan pada anggota, selain pemberian pinjaman? *(What kind of other services do you give to your members, besides loans?)*
    - ❑ Tabungan. *(Savings deposits)*
    - ❑ Pelatihan pembukuan. *(Training book keeping skills)*
    - ❑ Pelatihan Manajemen/Organisasi. *(Training management/organizational skills)*
    - ❑ Pelatihan Kewirausahaan. *(Entrepreneurship)*
    - ❑ Semua yang disebutkan di atas. *(All of the above)*
    - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

43. Berapa kali dalam setahun pelatihan tersebut diberikan? *(How many times in a year are trainings organised?)*
    ………………………………………………………………………………
    ……………………………………………………………………

44. Batuan apa saja yang anda terima dari LPKM, diluar pinjaman? *(What kind of help do you receive from LPKM, besides loans?)*
    - ❑ Pelatihan Pembukuan. *(Training book keeping skills)*
    - ❑ Pelatihan Manajemen/Organisasi. *(Training management/organizational skills)*
    - ❑ Pelatihan Kewirausahaan. *(Entrepreneurship)*
    - ❑ Semuanya yang disebutkan di atas. *(All of the above)*
    - ❑ Lain-lain (sebutkan),…………………………………… (*Other*)

45. Apakah anda berharap dapat menerima jenis pertolongan/pendampingan yang lain dari LPKM? *(Would you like to receive more help from LPKM?)*
    - ❑ Tidak *(No)*
    - ❑ Ya *(Yes)*

46. Bilamana jawaban anda Ya, maka jenis pertolongan/pendampingan apa yang anda harapkan dari LPKM-UNPAR? (*If yes, what other kind of help would you like to receive from LPKM?)*
    ………………………………………………………………………………
    ………………………………………………………………………………
    ………………………………………………………………………………
    ……………………………………………………………………

47. Apakah anda mengumpulkan/mencari informasi dari anggota Lembaga Keuangan/Koperasi tentang? (*Do you gather information from your members about?)*
    - ❑ Peningkatan pemasukan anggota Lembaga/Koperasi. (*Increased income of members)*
    - ❑ Ekspansi bisnis/investasi bisnis. (*Expansion of the business (investments in the business)*
    - ❑ Peningkatan kekayaan. (*Increased wealth)*

- Peningkatan daya beli. *(Increased consumption)*
- Peningkatan pendidikan dan gizi anak-anak anggota Lembaga/Koperasi. *(Members children receive more education/nutrition.)*
- Increased self esteem
- Menabung. *(Savings)*
- Peningkatan kemampuan bisnis (pembukuan, manajemen, dll.). (*Increased business skills (book keeping, management, et cetera)*

TERIMA KASIH ATAS KERJASAMANYA.
(THANK YOU FOR YOUR COOPERATION).

Appendix C Funding

Table C.I financial source

Financial source (amounts in Rupiah)	
Foundation of UNPAR, Pencairan	50,000,000
Foundation of UNPAR, Pencairan - 20 July 1998	30,000,000
Collaboration with local government - Jawa Barat	2,615,450
Vice Rektor III	2,500,000
Teacher of Architecture, 14 May 1998	3,500,000
Teacher of Architecture, 7 August 1998	3,500,000
Ibu Elsye (teacher at Economic Faculty UNPAR)	500,000
Bpk. Korniatmanto (teacher at Law Faculty UNPAR)	666,400
Collaboration with local government I	21,891,727
Ibu Benny Soeprapto	2,500,000
Collaboration with local government for area development	15,000,000
Charity NGO, Canada, CIDA	3,120,000
Collaboration with local government for research issues	10,190,452
Loan from university (outstanding amount)	20,000,000
Grand from local government (Bapede: Program Kejasama Pelatihann).	15,128,020
Bank account (Dapen)	2,190,000

Source: LPKM

The amounts listed in Table C.I are the amounts given in the past by the people and the organisations. Hence, it is not the amount outstanding, except for the loan from the university. Since LPKM had not enough liquidity, they asked the university for funding in order to prevent problems with payments. The interest rate on this loan is 0 per cent, with a loan term of four months. In the past LPKM did research and gave information to the local government on area development, empowerment of people, capitalism, local leadership, liberalism, and microfinance. Therefore, the local government passed a part of their budget to LPKM.

Dana Pendidikan (Dapen) requires specific attention. This is an account that belongs to Rismansyah and Rachmanto (two employees at LPKM). The money they receive from activities (e.g. when they are hired by the International Labour Organisation to arrange a workshop or lectures to students about empowerment of people) outside their normal job description is put into this account. When LPKM does not have enough financial resources and the microfinance institutions hand in a good loan proposal, this account can serve as a lender of last resort. No interest rate is charged for loans from this account. The initial purpose of this account however is to finance the *personal education needs* of the staff of the microfinance institutions. The education can be very broad since there are no criteria used when appealing to this account, even an education that has nothing in common with running a microfinance institution can be financed from this source. The borrower bears full responsibility for the personal loan, the microfinance institution is never liable for the loan (LPKM can never call upon the capital of the microfinance institution to recover the loan). In case the staff member defaults, the salary earned at the microfinance institution will be directly transferred to the Dapen account.

Appendix D Repayment

To determine repayment performance there are many useful indicators from which a choice can be made. However, the choice of an indicator depends among other things on the objective of the user. The reason why we presented the repayment rates of the microfinance institutions is that it is reasonable to expect a relation between the financial performance and the success of the microfinance institutions to adhere to the established micro credit principles. We calculated the repayment rate using the following formula, since the alternatives are not conclusive and comprehensive:

$$repayment\ rate\ including\ \ past\ due = \frac{collection\ on\ current\ amounts\ due + past\ due - \ prepayments}{total\ current\ amounts\ due + past\ due\ amounts}$$

Repayment rates using this formula cannot be higher than 100 per cent. This formula removes the effect of prepayments and shows the actual rate of received payments against expected payments on time and takes into account past due amounts. Therefore, this formula provides useful information on the performance of the microfinance institutions.

	BMW Bandung	Kopma ba	Mitra Sejahtera	Mitra Mandiri	Multi Usaha	Tatali Wargi	Mega Prima	Cib. Sebelas	BMW Sumadang	Nurul Amal	Kowardes Berkah
Collection of current amounts due + past due – prepayments											
May/June/July	3,210	2,385	945	0	2,564	1,058	520	217	1,200	173	351
Aug/Sept/Oct	5,933	712	945	726	2,165	1,544	346	651	1,036	173	1,045
Nov/Dec/Jan	6,975	1,041	1,891	1,089	1,308	2,532	693	651	349	0	1,479
Feb/March/April	4,733	1,719	1,891	1,089	0	5,602	519	1,171	0	0	1,102
Current amounts due											
May/June/July	3,210	3,485	945	0	2,651	1,058	520	217	900	346	351
Aug/Sept/Oct	5,933	1,812	945	726	4,471	1,838	520	651	1,685	520	1,045
Nov/Dec/Jan	7,353	1,916	1,891	1,089	4,683	3,356	520	651	1,947	520	1,479
Feb/March/April	7,224	2,619	1,891	1,089	3,949	4,310	519	1,171	1,947	520	1,870
Past due amounts											
May/June/July	0	50	0	0	582	0	0	0	300	0	0
Aug/Sept/Oct	0	1,150	0	0	668	0	0	0	0	173	0
Nov/Dec/Jan	0	2,250	0	0	2,887	294	173	0	349	521	0
Feb/March/April	377	3,124	0	0	4,923	1,118	0	0	1,947	1,041	0

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